Research Project

Convergence, competition, harmonisation – a comparative analysis of taxation in the Benelux states (1945-1992)

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"The fiscal history of a people is above all an essential part of its general history."

Joseph Schumpeter, 1972

"In this world nothing can be said to be certain, except death and taxes."

Benjamin Franklin, 1789

Structure

1. Introduction to the notions of fiscal policy and taxation

2. Sources of fiscal policy and their relative primacy

3. Introduction to the notion of tax competition

4. Taxation in the Benelux states – a historical overview

5. The research project (objective, research questions, deliverables, timetable)

1. Introduction to the notions of fiscal policy and taxation

Fiscal policy: a complex, constantly developing process that reflects the relationship between the state and society from the specific angle of taxation.

Taxation:

- is a term with many meanings and uses
- is a multidimensional concept (political, economic, social, state-citizen relationship, relations between countries, etc.)
- is always viewed from the perspective of “income/expenditure”, as governed by a budget

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1. Introduction to the notions of fiscal policy and taxation

Types of taxation:

- **direct** (permanent and recurrent, collected directly from citizens and applied to revenue, capital, business profits, etc. Social security contributions are also a form of direct taxation)

- **customs duties** (applied to goods entering or leaving a specific customs territory) and **excise** (alcohol, tobacco, mineral oils, etc.)

- indirect taxation (for acts and deeds conducted on a regular or occasional basis, such as transfers of ownership and business transactions, including VAT)

Summary
"The verbs "to be" and "to have" refer to direct taxation, and the verb "to do" refers to indirect taxation."
René Stourm, 1912

1. Introduction to the notions of fiscal policy and taxation

Characteristics of taxation:

- it must be fair and equitable

- it must not be arbitrary

- it must be raised in a convenient way for the taxpayer

- it must not exceed the strict minimum needed

- it must be legal and collected with consent

Consent to taxation has a twofold meaning: first, it is **the rule** according to which taxation may be collected only with the consent of the nation's representatives, and second, it refers to the "**individual psychological acceptance** of the taxpayer" (Beltrame 1995). From this perspective, taxation – especially personal and income tax – may be seen by some as an "**injustice**", an "impoverishment", an "act of plunder" or "confiscatory practice" (Kirschler, 2007). This has given rise to a **temptation to explore means of "tax deviance"** – in other words eluding taxation by **evasion** or **tax fraud** (Becker, 1963).

2. Sources of fiscal policy and their relative primacy

A country's approach to taxation is shaped by its history, customs and traditions, its specific characteristics and its degree of regional and international integration.

Parameters for analysis:
- political sovereignty – fiscal sovereignty
- juxtaposition of fiscal sovereignties

Sources of fiscal policy:
- the state (states)
- international, bilateral and multilateral arrangements

Primacy:
- Although in principle **international tax law takes precedence** over national law, **it does not replace national law** and only applies in specific areas.

- Given that **direct taxation falls within the exclusive remit of individual states**, national (tax) law is generally applicable.

Phenomena observed in the area of taxation: introduction of "**tax loopholes**" and "**tax optimisation**" practices, which generate (mostly **harmful**) **tax competition** between countries.

3. Introduction to the notion of tax competition

Tax competition is defined as competition between **different legal systems** which have the privilege of raising taxes and which attempt to attract a mobile tax base. This type of competition may occur between legal systems at the same level, namely states (horizontal competition), or between two legal systems at different levels which raise taxes on the same tax base (e.g. a federal and regional level – vertical competition).

Origins
The notion of tax competition emerged in the United States in the 1950s, at a time of growth in public budgets – the 1956 Tiebout model (optimum provision of goods).

The state chooses a system of taxation in line with an "optimisation programme", which involves maximising its preferences.

3 types/models of state:

- **the benevolent state** – which adopts a benevolent approach in a bid to improve the well-being of its citizens. Tax competition acts as a brake on economic efficiency (Bucovetsky, 1991; Wilson, 1991).

- **the Leviathan state** – which tries to maximise tax revenue and the efficiency of public spending (Brennan & Buchanan, 1980).

- **the moderate Leviathan** – which attempts to maximise the well-being of citizens but tends towards inefficient spending of tax revenue (Edwards & Keen, 1996).

3. Introduction to the notion of tax competition

The typology above demonstrates the **inequality of states in the area of tax competition.**

This results in two types of tax competition among states, one that can be referred to as "fair" or "acceptable", and one that is seen as "harmful" or "damaging". The line between the two broadly reflects the distinction between general reductions in taxation as desired by citizens (who are both voters and taxpayers) and tax reductions granted exclusively to foreign investors. Economic integration between states initially reduces the intensity of tax competition, before subsequently increasing it (Bretin, 2002).

To combat harmful tax competition, the OECD, followed by the EU, established a broad framework for reflection. While their spheres of action differ, their criteria for identifying harmful tax competition are very similar. **The main criterion** – namely, a much lower level of taxation than the normal level applied in the state concerned – can be used to pinpoint any (potentially) harmful practices (OECD, 1998).

Secondary criteria then come into play, such as the absence of transparency with regard to the exchange of information on preferential regimes. But these criteria only apply to measures that give rise to "obvious distortions" (Hugounenq, Le Cacheux & T. Madiès, 1999).

4. Taxation in the Benelux states – a historical overview

4.1. Benelux relations at a glance

Luxembourg's geographical position, political and national development and changing statehood have always linked it closely with the Netherlands, Belgium, Germany and France.

4.2. An outline of sources of taxation in the Benelux

Luxembourg

Indirect taxation
- duties on spirits and inheritance (origins in Dutch legislation)
- registration duties, stamp duties and mortgage duties (origins in French legislation)
- customs and excise duties (origins in Belgian legislation, then BLEU and Benelux)
- turnover tax (*Umsatzsteuer*) (origins in French then German legislation)

Direct taxation
- **personal contribution**, **patent duty** and **property tax** (origins in Dutch legislation) (1839-1849)
- 1849 – these taxes replaced by the **personal contribution** (schedular system on income)
- 1919 – introduction of a **general income tax** grouping together all previous direct taxes. Introduction of a **"minimum subsistence exemption"** (Susini, 1922).

4. Taxation in the Benelux states – a historical overview

Luxembourg's occupation by the Nazi army in May 1940 resulted in its traditional laws being replaced by corresponding German provisions, via a number of *Verordnungen* (decrees).

Impact on the tax system:

- **18 July 1941 – introduction of the German system** of taxes, levies, contributions and duties, which applied to all categories of taxpayer (this system continued to operate after Luxembourg's sovereignty was restored).

- **26 October1944** – Grand-Ducal decree confirming that German direct taxation would be maintained (although various discriminatory clauses were removed) and replacing indirect taxation by the taxes in place in Luxembourg before the Occupation. Taxes and social contributions would become a major means of redistribution within the welfare state.

Reforms:

- **4 December1967** – Law on Income Tax

- **early 1990s** – "constant reformism"

  * **Direct taxation** – adaptation of the tax system for the purposes of balancing public finance

  * **Indirect taxation** – meeting OECD and EU demands for harmonisation

5. The research project (objective, research questions, methodology and sources, deliverables, provisional timetable)

5.1 The aim – to perform a comparative historical analysis of the development and specific characteristics of taxation in Luxembourg, as developed in a multidimensional context – national (Luxembourg), regional (relations with traditional partners Belgium and the Netherlands but also Germany and France), European (ECSC, EEC and EU) and international (OECD, GATT/WTO) – in the second half of the 20th century.
The two aspects of taxation will be addressed: direct taxation (a prerogative of states) and indirect taxation (subject to international regulation).

5.2. The timeframe stretches from the end of the war (1944) to the Maastricht Treaty (1992). Why?

5.3. Main **research questions** – 4 areas:

- how did theoretical and political debates on taxation develop during the period under analysis? How do theoretical apparatuses relate to actual tax systems?

- states' fiscal policy, the importance of international relations (national interests, power play, the limits of multilateralism), bilateral and multilateral regulation (OECD, EU, WTO)

- how was Luxembourg's tax system developed (as influenced by Belgium, the Netherlands, Germany and France)?

- by way of conclusion – projections on the future of taxation in Luxembourg

5. The research project (objective, research questions, methodology and sources, deliverables, provisional timetable)

5.4. Methodology and sources

- Public and private archives
- A series of interviews – oral history
- Specialised literature

5.5 Expected results

- Production of a written analysis on the subject, accompanied by a selection of relevant sources, a comprehensive and regularly updated bibliography, a chronology and a glossary of terms related to taxation

- International conference (2021) and publication of proceedings

5.6. Provisional timetable

- project length – 3 years (2019, 2020, 2021)
- outreach and application of research results (from 2021 onwards)