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The Impact of European Integration on the Tax Systems of European Union Member States

Abstract: The organisation of the tax system and the definition of tax policy are determined by each state in its own way, depending on all the significant factors that characterise that state. However, within the single internal market of the European Union, Member States should pursue tax policies that move in broadly similar directions, since the activities and measures undertaken by one country may have an impact on neighbouring and other countries. In this respect, the European Union plays only a supporting role, and its objective is not to "standardise" national tax systems, but rather to ensure that they are compatible not only with one another, but also with the objectives laid down in the Treaty establishing the European Community. Given that taxes, from the perspective of the subject matter of taxation, may constitute a barrier to the implementation of the fundamental principles of free trade and the basic elements of the internal market, the need arose for the harmonisation (alignment) of certain tax laws of European Union Member States, as well as of countries committed to accession to the European Union.

Key Words: internal market, tax competition, European Union law.

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1. INTRODUCTION

The tax system and tax policy represent one of the key attributes of a state's national sovereignty.[1] The extent to which a state will impose taxes, what it will tax, and whom it will tax are matters determined exclusively by democratic political choices within that state. The tax systems of modern states differ from one another. The reasons for the diversity of each state's tax system should be viewed in the context of the state's organisation and the influence of all factors characterising that state, including its socio-economic system, level of economic development, degree of economic openness, labour force structure, educational attainment of the population, and membership in particular regional groupings. Nevertheless, despite the fact that diversity is a fundamental characteristic of tax systems

[1] For further details, see: Gordana Ilić-Popov, European Union Tax Law, "Official Gazette", Belgrade, 2004, p. 11.

and that every state has the right to determine the structure of its tax system and the essential elements of each type of tax, the question arises as to how such diversity fits into the integration processes that constitute a defining feature of the era in which we live. One of the fundamental objectives of European integration is the establishment of an internal market, which represents the very essence of today's European Union. It should be borne in mind that the foundations of the European Union's internal market were laid down by the Treaty establishing the European Economic Community.[2] Article 2 of the Treaty provides, inter alia: *"The Community shall have as its task, by establishing a common market and an economic and monetary union and by implementing the common policies and activities referred to in Articles 3 and 4, to promote throughout the Community a harmonious, balanced and sustainable development of economic activities, a high level of employment and social protection, equality between men and women, sustainable and non-inflationary growth, a high degree of competitiveness and convergence of economic performance, a high level of environmental protection and improvement of the quality of the environment, the raising of the standard and quality of life, and economic and social cohesion and solidarity among Member States"*.[3] The creation of the internal market implies not only the liberalisation of trade among Member States, but also the liberalisation of the movement of factors of production: goods, capital and services, while respecting the principles of competition policy.[4] This, in turn, entails the freedom of establishment for individuals and business entities throughout the territory of the Member States.

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[2] The Treaty establishing the European Economic Community was signed in Rome in 1957, together with the Treaty establishing the European Atomic Energy Community (the Rome Treaties). The signatory states were the countries that had signed the 1951 Paris Treaty establishing the European Coal and Steel Community (West Germany, France, Italy, Belgium, the Netherlands and Luxembourg). The Treaty established a Customs Union among the Member States of the European Economic Community and set the objective of creating a common European market within which the free movement of persons, goods, services and capital would be ensured. All subsequent amendments to the founding treaties were aimed at achieving the objectives established by those treaties. For further details, see: Professor. Milorad Bodiroža, European Union, Second Revised Edition, Glas Srpske, Grafika, Banja Luka, 2006, p. 330.

[3] Dr. Duško Lopandić, The Founding Treaties of the European Union, Office for the Accession of Serbia and Montenegro to the European Union, European Movement in Serbia, Belgrade, 2003, p. 47.

[4] Competition policy is one of the fundamental elements of the internal market and is based on the understanding that economic activity must be founded upon the principles of a market economy and fair competition. The legal framework in the field of competition began to take shape during the earliest stages of the European integration process and is founded upon Articles 81–90 of the Treaty establishing the European Community. In this regard, one of the requirements set out in the Road Map for Bosnia and Herzegovina and in the Feasibility Study was the adoption of the Competition Act of Bosnia and Herzegovina and the full alignment of that Act with European Union standards, which subsequently led to the establishment of the Competition Council responsible for the implementation and monitoring of competition policy. For further details, see: Training Manual on European Union Integration, p. 86.

2. SOURCES OF TAX HARMONISATION

The general approach of the European Community, as reflected in the Community's founding treaties[5], is that taxation has traditionally been linked to the issue of national sovereignty. While the European Community does not have the authority to impose taxes or other public charges, a certain degree of tax harmonisation is nevertheless required in order to preserve and develop the values of the internal market. Harmonisation entails the alignment of the different tax regulations of Member States, but only to the extent necessary for the functioning of the internal market.[6]

Within the European Union, the harmonisation of tax systems and tax policies has three principal sources:

1) the provisions of the founding Treaty itself;

2) tax competition among Member States, which leads to spontaneous harmonisation; and

3) the prohibition of discrimination against goods, services, capital, undertakings and workers from other Member States.

2.1. PROVISIONS OF THE FOUNDING TREATY AND TAX HARMONISATION

The Founding Treaty contains several groups of provisions that give rise to the need for tax harmonisation. The first group consists of provisions deriving from the customs union upon which the European Community is founded[7].

The second group of provisions[8] is significant for the harmonisation of indirect taxation. These provisions stipulate that the harmonisation of indirect taxes is a prerequisite for the establishment and smooth functioning of the Union's internal market and therefore confer powers upon the Union institutions to adopt directives in this field. In this context, all Member States, in accordance with numerous directives of the EC Council, introduced value added tax (VAT), with harmonised definitions of the taxable person, taxable event, tax base, tax reliefs, the tax credit mechanism, and a minimum tax rate of 15%. Border controls in "intra-Community transactions" (i.e. supplies of goods and services where the supplier is located in one Member State and the purchaser in another) were abolished, and the excise duty system was harmonised.

The third group[9] of provisions governs the harmonisation of national legislation in

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[5] Article 58, Article 90, Article 91, Article 92, Article 93 and Article 132 of the Treaty establishing the European Economic Community.

[6] Article 93 (formerly Article 99) of the Treaty establishing the European Community provides as follows: "Acting unanimously on a proposal from the Commission and after consulting the European Parliament and the Economic and Social Committee, the Council shall adopt measures for the harmonisation of legislation relating to turnover taxes, excise duties and other forms of indirect taxation, insofar as such harmonisation is necessary for the establishment of the internal market."

[7] Articles 23–31 (formerly Articles 9, 10, 12, 28, 29, 30, 34, 36 and 37) of the Founding Treaty prohibit the introduction of any import or export customs duties or other charges having equivalent effect between Member States.

[8] Articles 90–93 of the Founding Treaty (formerly Articles 95, 96, 98 and 99) concern the harmonisation of indirect taxes, namely general turnover taxes and excise duties.

[9] Article 94 of the Founding Treaty (formerly Article 100 and, to a certain extent, former Article 235 of the Founding Treaty).

general, to the extent necessary for the establishment and functioning of the single market. Since the Founding Treaty makes no specific reference to harmonisation in the field of direct taxation, the powers of the relevant Union institutions to adopt directives providing for a certain degree of alignment of direct taxes have been derived from Article 94 of the Treaty, which addresses the harmonisation of legislation *en general*.

2.2. TAX COMPETITION AS A SOURCE OF HARMONISATION

Tax competition among Member States leads to the spontaneous convergence of national tax laws, as factors of production are generally directed towards the economies of those Member States whose tax systems are more favourable and stimulative. As a result, Member States are encouraged to adapt their fiscal regulations to those in force in countries that have succeeded in attracting capital through more favourable tax solutions. In this way, significant tax differences among Member States gradually diminish, while tax competition may contribute to the establishment of a more efficient tax system, since each country can draw upon the positive experiences of others.

2.3. PROHIBITION OF DISCRIMINATION AGAINST GOODS FROM THIRD COUNTRIES

The achievement of the Union's fundamental objectives, namely the establishment of a single internal market and the increasingly close alignment of the economic policies of the Member States, presupposes so-called negative integration. Negative integration is reflected in prohibitions on conduct that would undermine the four fundamental freedoms upon which the Union is based. This includes the prohibition of discrimination on grounds of nationality or the origin of goods, services and capital. Given that Member States have, in practice, retained fiscal sovereignty in the area of direct taxation, it is in principle possible for national tax legislation to result in discrimination, for example by distinguishing between resident and non-resident taxpayers. When considering sources of harmonisation from the perspective of the prohibition of discrimination against goods from third countries, it should be emphasised that the European Court of Justice has had a significant influence on the formulation of the tax policies of Member States. It is regarded as one of the most effective institutions of the Community in removing tax obstacles to the unhindered conduct of cross-border economic activities within the Union. In judicial proceedings, the European Court of Justice directly applies the "four freedoms", and the consequence of this approach is that provisions of national tax law that fail to prohibit discrimination against goods from third countries or discrimination on grounds of nationality are frequently set aside and rendered inapplicable.[10]

3. AREAS OF HARMONISATION

Harmonisation in the field of tax policy and tax systems may be viewed in relation to:
1. harmonisation in the field of indirect taxation;
2. harmonisation in the field of direct taxation; and

[10] At conferences of EU officials, it was concluded that certain EU Member States (Spain, Italy, Portugal and Austria) have, in some cases, disregarded the impact of judgments adopted by the European Court of Justice concerning various disputed issues and instances of tax barriers. See, in this regard: Joann Weiner, European Officials Consider Importance of Coordinating EU Company Tax Policies, 32 Tax Notes International (15 December 2003), p. 1001.

3. harmonisation in the field of tax cooperation.

3.1. HARMONISATION IN THE FIELD OF INDIRECT TAXATION

To date, the legislative activity of EU institutions has been most intensive in the field of indirect taxation, namely general turnover tax – value added tax (hereinafter: VAT) – and excise duties. The process of harmonising indirect taxes, based on the provisions of Article 99 of the Treaty, encompasses the measures necessary to ensure the establishment and functioning of the internal market through the removal of all obstacles to the free movement of goods and services.

3.1.1. HARMONISATION OF GENERAL TURNOVER TAX

The first phase of the harmonisation of general turnover tax was completed through the adoption and implementation of Directive 77/388/EEC on the harmonisation of the turnover tax laws of the Member States[11], together with several subsequent implementing directives. This directive, better known as the Sixth Directive, is regarded as the "basic EU law in the field of VAT" because it ensured the harmonisation of all the most important elements of the legal framework governing VAT, including the taxable person, taxable transactions, the tax base, tax exemptions, the right to deduct input tax, and other key elements.

In addition to the aforementioned VAT Directive, the following directives are also of particular significance:

The Directive on the abolition of fiscal barriers[12], which fundamentally altered the VAT regime applicable to intra-Community transactions established by the Sixth Directive. Under the provisions of this Directive, the supply of goods and the provision of services from one Member State to another are no longer regarded as exports and imports respectively, while border controls between Member States were abolished with effect from 1 January 1993.

The Directive on the simplification of procedures during the transitional period[13] was intended to simplify the assessment and collection of VAT in relation to intra-Community transactions during the transitional period. In this regard, taxation was deferred until the first supply made by the importer, rather than being levied at the time of importation.

The Directive on the approximation of VAT rates[14] aims to bring VAT rates in the Member States closer together. The standard VAT rate applicable in all Member States was established on the basis that, during the transitional period, it could not be lower than 15%. Higher rates were abolished, while the application of one or, at most, two reduced

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[11] Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes – Common system of value added tax: uniform basis of assessment, Official Journal L 145 of 13 June 1977.

[12] Council Directive 91/680/EEC of 16 December 1991 supplementing the common system of value added tax and amending Council Directive 77/388/EEC with a view to the abolition of fiscal frontiers, Official Journal L 376 of 31 December 1991.

[13] Council Directive 92/111/EEC of 14 December 1992 amending Council Directive 77/388/EEC and introducing simplification measures with regard to value added tax, Official Journal L 384 of 30 December 1992.

[14] Council Directive 92/77/EEC of 19 October 1992 supplementing the common system of value added tax and amending Council Directive 77/388/EEC (approximation of VAT rates), Official Journal L 316 of 31 October 1992.

rates was permitted, provided that such reduced rates were not lower than 5%. These may be applied only to supplies of goods and services expressly listed in a specific annex, including food products, water, medicines and medical equipment, passenger transport, books and other publications, cultural and sporting services, supplies of goods and services in agriculture (excluding capital goods), social welfare and social security services, as well as funeral services and related equipment.

The Directive on VAT in electronic commerce[15], adopted in mid-2002, was intended to eliminate distortions in market competition and to ensure legal certainty, simplicity and neutrality within the tax system. Accordingly, transactions involving the supply of goods and services should be taxed in the same manner regardless of the method through which trade is conducted, that is, irrespective of whether supplies are made online or offline. Furthermore, taxation rules must take account of technological developments in the provision of services in order to prevent losses in tax revenue and avoid distortions of competition. The essence is to ensure compliance with the fundamental principle established by the Sixth Directive, namely that services are taxed in the place where the service provider is established. Since VAT is reflected in the final selling price of goods and services whenever it is charged, the Directive introduced a requirement that companies established outside the territory of the EU which provide online services to customers in EU Member States must register for VAT purposes and obtain a VAT identification number within the EU.

3.1.2. HARMONISATION OF EXCISE DUTIES

The common excise duty system in the European Union entered into force on 1 January 1993, when the single market began operating. It encompasses selective consumption taxes on mineral oils, tobacco products and alcoholic beverages. The rationale for prescribing these "mandatory" excisable products lies in the fact that they are goods whose consumption guarantees substantial tax revenues. Member States may also introduce excise duties on certain other products (where justified by fiscal, economic, environmental or other considerations), provided that such measures do not entail additional formalities in the cross-border movement of those goods and are not associated with increased administrative costs.

Community rules governing excise duties encompass: a harmonised tax structure (the definition of excisable products, determination of the tax base and tax exemptions); tax rates (the establishment of minimum tax rates, while allowing Member States the discretionary right to introduce their own excise duty rates, taking account of the international environment); and the movement of excisable products between Member States (the excise warehouse regime).

The harmonisation of excise duties within the EU framework is based on a number of directives, which may be divided into three groups.

1) The first group consists solely of the Directive on the general arrangements for products subject to excise duty and on the holding, movement and monitoring of such products, commonly known as the "Horizontal Directive"[16]. This Directive provides that

[15] Council Directive 2002/38/EC of 7 May 2002 amending and amending temporally Directive 77/388/EEC as regard the value added tax arrangements applicable to radio and television broadcasting services and certain electronically supplied services, Official Journal L 128 of 15 May 2002.

[16] Council Directive 92/12/EEC of 25 February 1992 on the general arrangements for products

the tax liability, as a general rule, arises at the moment of production of the goods or upon their importation into the territory of the Union, while leaving it to Member States to determine the rules governing the production, processing and storage of products subject to excise duty. Importation is defined as the entry of an excisable product into the territory of the European Union. Member States may require products released for consumption within their territory to bear so-called excise stamps[17], provided that the use of such stamps does not impede the free conduct of trade or the free movement of excisable goods between Member States. The taxation of excisable products is based on the destination principle, thereby ensuring that exports are not subject to taxation.

The Horizontal Directive also provides for exemptions from excise duty in cases involving supplies of excisable products to diplomatic and consular missions, international organisations and members of such organisations (subject to certain limits and restrictions), supplies made to the armed forces of Member States, and other similar situations.[18]

2) The second group comprises the "Structural Directives"[19] on the harmonisation of the structure of excise duties applicable to mineral oils, alcoholic beverages and tobacco products. The Structural Directive on mineral oils establishes a uniform definition of thirteen different categories of mineral oil products. It provides that excise duty rates shall be specific in nature, while the corresponding Rates Directive (92/82/EEC) prescribes minimum rates for only seven of the thirteen categories of mineral oils. These rates may not fall below specified amounts (for example, 337 ECU per 1,000 litres of leaded petrol; 287 ECU per 1,000 litres of unleaded petrol; 100 ECU per 1,000 litres of liquefied gas, etc.). The Council of the Community is required periodically to review the minimum excise duty rates and tax exemptions, taking into account the need to ensure the "smooth functioning of the Community's single market, realistic excise duty levels, and the broader objectives

subject to excise duty and on the holding, movement and monitoring of such products (Horizontal Directive), Official Journal L 076 of 23 March 1992.

[17] See, for example: Council Directive 95/60/EC of 27 November 1995 on fiscal marking of gas oils and kerosene, Official Journal L 291 of 6 December 1995. See also: Commission Decision 2001/574/EC of 13 July 2001 establishing a common fiscal marker for gas oils and kerosene, Official Journal L 203 of 28 July 2001; Commission Decision 2002/269/EC of 8 April 2002 amending Decision 2001/574/EC establishing a common fiscal marker for gas oils and kerosene, Official Journal L 093 of 10 April 2002; Commission Decision 2003/900/EC of 17 December 2003 amending Decision 2001/574/EC establishing a common fiscal marker for gas oils and kerosene (notified under document number C(2003)4607), Official Journal L 336 of 23 December 2003.

[18] Commission Regulation (EC) No. 31/96 of 10 January 1996 on the excise duty exemption certificate, Official Journal L 008 of 11 January 1996.

[19] Council Directive 92/78/EEC of 19 October 1992 amending Directives 72/464/EEC and 79/32/EEC on taxes other than turnover taxes which are levied on the consumption of manufactured tobacco, Official Journal L 316 of 31 October 1992. Council Directive 92/81/EEC of 19 October 1992 on the harmonisation of the structures of excise duties on mineral oils, Official Journal L 316 of 31 October 1992. This Directive ceased to have effect on 1 January 2004 upon the entry into force of Council Directive 2003/96/EC of 27 October 2003 restructuring the Community framework for the taxation of energy products and electricity, Official Journal L 283 of 31 October 2003. Council Directive 92/83/EEC of 19 October 1992 on the harmonisation of the structures of excise duties on alcohol and alcoholic beverages, Official Journal L 316 of 31 October 1992.

established by the Founding Treaty." The Structural Directive on mineral oils also contains provisions relating to tax exemptions, which may be either mandatory (for example, fuel used for commercial air transport and maritime shipping) or optional (for example, fuel with favourable environmental characteristics).[20]

The Structural Directive on alcoholic beverages distinguishes among various categories of beverages, including beer, wine, spirits and other alcoholic drinks. Specific duty rates are prescribed, based on the Plato hectolitre degree, together with their minimum amounts. The Directive permits Member States to apply reduced excise duty rates to beer, provided that such rates are not lower than 55% of the standard rate applicable in the Member State concerned, depending on the annual beer production of the brewery in question. A tax concession in the form of a reduced excise duty rate may be granted only to breweries producing less than 200,000 hectolitres of beer annually (so-called small breweries). Member States may also exempt from excise duty beer produced by a natural person, provided that it is consumed by the producer, members of the producer's family, or the producer's guests, that is, where the beer is intended for personal consumption. Under the Structural Directive on alcoholic beverages, wine is likewise subject to taxation. A distinction is made between still wines and sparkling wines, while the Plato hectolitre degree of alcoholic strength is also used as the basis for taxation.

Particular importance attaches to the directives governing excise duties on tobacco products, which provide definitions for various categories of tobacco products, including cigarettes, cigars and cigarillos, fine-cut tobacco for rolling cigarettes, and pipe tobacco. Effective collection of cigarette taxes requires close cooperation between the state and cigarette manufacturers or importers. Governments and the competent authorities of Member States enjoy considerable discretion in determining the procedures for collecting cigarette taxes. However, they must comply with the following fundamental requirements established by the European Union: collection procedures must be applied equally to all cigarette manufacturers and importers (the non-discrimination clause); and the ad valorem excise duty must be calculated on the basis of the maximum retail selling price determined by the manufacturer or importer.

3) The third group consists of directives concerning the approximation of excise duty rates applicable to mandatory excisable products, commonly referred to in practice as the Rates Directives.[21]

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[20] Council Decision 2001/224/EC of 12 March 2001 concerning reduced rates of excise duty and exemptions from such duty on certain mineral oils when used for specific purposes, Official Journal L 084 of 23 March 2001..

[21] Council Directive 92/79/EEC of 19 October 1992 on the approximation of taxes on cigarettes, Official Journal L 316 of 31 October 1992.
Council Directive 92/80/EEC of 19 October 1992 on the approximation of taxes on manufactured tobacco other than cigarettes, Official Journal L 316 of 31 October 1992.
Council Directive 92/80/EEC of 19 October 1992 on the approximation of the rates of excise duties on mineral oils, Official Journal L 316 of 31 October 1992. This Directive ceased to have effect on 1 January 2004, upon the entry into force of Council Directive 2003/96/EC of 27 October 2003 restructuring the Community framework for the taxation of energy products and electricity, Official Journal L 283 of 31 October 2003.
Council Directive 92/84/EEC of 19 October 1992 on the approximation of the rates of excise duty on alcohol and alcoholic beverages, Official Journal L 316 of 31 October 1992

3.2. HARMONISATION IN THE FIELD OF DIRECT TAXATION

With a view to harmonising direct taxation, the European Union has adopted a number of directives and recommendations relating to personal income taxation, the taxation of companies, and the avoidance of double taxation.

1) In the field of **personal income taxation**, the EU has adopted two recommendations, of which the *Recommendation on the Tax Treatment of Non-Resident Individuals*[22] is regarded as particularly significant. It is based on three fundamental principles:

- Non-resident individuals must enjoy the same tax treatment as residents of the Member State in whose territory they are employed or carry on a business activity, provided that at least 75% of their total income is earned in that State;
- The State of residence may refuse to grant tax reliefs (deductions or tax credits) to its residents who earn income abroad if they already benefit from equivalent reliefs in the Member State where they carry out their business activity;
- The Recommendation applies only to the so-called "active" income of individuals (salaries and wages, or income derived from self-employment).

In addition to the above Recommendation, the Recommendation on the Tax Treatment of Small and Medium-Sized Enterprises,[23] adopted in 1994, proceeds from the premise that partnerships are generally subject to the application of progressive corporate profit taxation and that this may seriously undermine tax neutrality as well as incentives for capital investment. Accordingly, the Recommendation calls upon Member States to consider granting small and medium-sized enterprises the option of being taxed under the corporate profits tax regime instead of the personal income tax[24] regime, or, at the very least, to examine the possibility of reducing personal income tax rates on that portion of profits that SMEs reinvest in their business activities.

2) In the field of the **taxation of corporate profits**, the EU pursues two principal objectives: to prevent harmful tax competition among Member States[25]; and to support the principle of the free movement of capital. To that end, the following measures have been adopted:

a) *The Directive on the tax treatment of dividends paid by a subsidiary to its parent*

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[22] Commission Recommendation 94/79/EC of 21 December 1993 on the taxation of certain items of income received by non-residents in a Member State other than that in which they are resident, Official Journal L 039 of 10 February 1994.

[23] Commission Recommendation 94/390/EC of 25 May 1994 concerning the taxation of small and medium-sized enterprises, Official Journal L 177 of 9 July 1994.

[24] The tax laws of Spain, Belgium and Greece, as well as France (on an optional basis), provide for the profits of partnerships to be taxed under the corporate profits tax regime. Gordana Ilić-Popov, op. cit., p. 143.

[25] In the past, Member States offered excessive tax incentives in order to attract foreign investors, often to the detriment and expense of other Member States in which the same investment would, from a purely economic perspective, have been more justified. In its Communication of 5 November 1997 entitled "A Package to Tackle Harmful Tax Competition in the European Union" (COM (97) 564 final), the European Commission emphasised the need for coordinated action at Union level in order to combat harmful and unfair tax competition, with a view to facilitating the achievement of objectives such as reducing persistent distortions within the internal market and preventing excessive losses of tax revenue in individual Member States. For further details, see: Gordana Ilić-Popov, op. cit., p. 127.

company[26]. In order to ensure the unrestricted distribution of dividends between companies where the parent company and the subsidiary are residents of different Member States, the Directive provides that the State of residence of the subsidiary may not impose withholding tax on dividends paid by the subsidiary to a parent company resident in another Member State. The State of residence of the parent company is permitted, for the purpose of avoiding double taxation, either to apply the exemption method, whereby received dividends are excluded from taxable profits, or to apply the indirect tax credit method, whereby the parent company may deduct from its corporate income tax liability the tax paid by the subsidiary in its State of residence on the profits out of which the dividends were distributed. For the indirect tax credit method to apply, the Directive requires the following conditions to be satisfied cumulatively:

- The company must be organised in one of the recognised forms of capital companies (joint-stock company, limited liability company, company limited by shares, etc.);
- The company must be a resident of the relevant Member State; and
- The company must be subject to the national corporate profits tax.

b) *The Directive on the tax treatment of corporate restructuring operations*[27] applies to mergers, divisions, transfers of assets and exchanges of shares.

c) The Code of Conduct for Business Taxation[28] constitutes primarily a political agreement among EU Member States rather than a legally binding instrument. Its purpose is to eliminate distortions of competition within the Union's internal market and to prevent the erosion of corporate tax bases. Member States are expected to adhere to the principles of fair competition and to refrain from introducing tax measures that could adversely affect economic activities conducted between EU Member States. The Code of Conduct provides for appropriate monitoring mechanisms designed to prevent the introduction or continued existence of harmful tax measures within the Union.

3) In the field of the **avoidance of double taxation**, the following instruments have been adopted: the Directive on the taxation of interest and royalty payments, the Directive on the taxation of savings income, and the Arbitration Convention.

The Directive on the taxation of interest and royalty payments[29] aims to abolish withholding taxes on interest and royalty payments made between associated enterprises that are residents of different EU Member States. In this way, economic double taxation

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[26] Council Directive 90/435 EEC of 23 July 1990 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States (Parent - Subsidiary Directive), Official Journal L 225 of 20 August 1990.

[27] Council Directive 90/434/EEC of 23 July 1990 on the common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares concerning companies of different Member States (Merger Directive), Official Journal L 225 of 20 August 1990. The full title of the Directive is: Directive on the common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares involving corporations from different Member States.

[28] The Code of Conduct for Business Taxation was published by the ECOFIN Council on 28 February 2000.

[29] 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, Official Journal L 157.

of this category of income is eliminated and the administrative costs borne by companies are reduced. The recipient of the interest or royalty payment may be either a company resident in another Member State or a permanent establishment located in another EU Member State.

The objective of the *Directive on the taxation of savings income*[30] is to ensure that savings income in the form of interest paid in one EU Member State to an individual resident in another Member State is subject to effective taxation in accordance with the legislation applicable in that latter Member State.

The Arbitration Convention[31] is essentially intended to establish a framework for coordination aimed at eliminating economic double taxation in transactions between two associated enterprises resident in different Member States, as well as in transactions between a head office and its branch where the head office is located in one Member State and the branch in another. The Arbitration Convention is not a legal (binding) instrument of the European Union; rather, it has the status of a multilateral convention under public international law and is intended to eliminate double taxation in the aforementioned cases.

4. HARMONISATION IN THE FIELD OF TAX COOPERATION

In the area of tax cooperation harmonisation, the Directive on Mutual Administrative Assistance between the Tax Authorities of Member States[32] was adopted. Its objective is to oblige Member States to exchange all information that may enable the accurate and proper assessment of income tax, property tax, VAT and excise duties. The Directive relates exclusively to the assessment of taxes and does not apply to the collection or recovery of taxes, nor to the exchange of documents. Information obtained under the Directive must be treated as official confidential information and may be disclosed only to persons directly involved in the assessment of the relevant taxes or in judicial or administrative offence proceedings undertaken for the purpose of ensuring the correct and most accurate determination of tax liabilities. Such information may not be disclosed to persons involved in any way in the collection of taxes or in the enforcement of administrative or criminal penalties.

The Directive also provides for certain circumstances in which a Member State may refuse to cooperate in the exchange of information, including where: the requesting State has not first exhausted all available means within its own territory to obtain the required information; the requested Member State would be required, in order to provide the information, to carry out investigations, enquiries or similar actions which it would not undertake even for its own purposes; the provision of the information would entail the disclosure of a commercial or professional secret; the disclosure of the information would be contrary to public policy or the public interest; and other comparable circumstances exist.

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[30] Council Directive 2003/48/EC of 3 June 2003 on taxation of savings income in the form of interest payments, Official Journal L 157 of 26 June 2003.

[31] Convention 90/436/EEC on the elimination of double taxation in connection with the adjustment of profits of associated enterprises (Arbitration Convention), Official Journal L 225 of 20 August 1990.

[32] Council Directive 77/799 EEC of 19 December 1977 concerning mutual assistance by the competent authorities of the Member States in the field of direct taxation, Official Journal L 336 of December 1977.

5. CONCLUSION

Tax policy and the organisation of a country's tax system are matters determined by each State individually, depending on its socio-economic structure, level of economic development, degree of economic openness, labour force structure, educational attainment of the population and membership in particular regional groupings. However, although the tax system and tax policy constitute an expression of a State's national sovereignty, and although every State independently decides what will be taxed, who will be taxed and to what extent, the process of European integration, viewed through the fundamental elements of the internal market and the free movement of factors of production, has created a need for the harmonisation of the tax systems and tax policies of European Union Member States, as well as of countries aspiring to membership of the European Union. The principal sources of tax harmonisation are the provisions of the Founding Treaty itself, tax competition among Member States leading to spontaneous harmonisation, and the prohibition of discrimination against goods, services, capital, undertakings and workers from other Member States. The most significant achievements in tax harmonisation have been made in the field of indirect taxation, since the taxation of supplies of goods and services is regarded as a non-tariff barrier that may restrict the free movement of goods and services within the internal market. For this reason, EU legislative activity has been most intensive in the harmonisation of the fundamental elements of general turnover tax – value added tax (VAT) –and excise duties as specific taxes imposed on the consumption of certain products. In this context, the introduction of value added tax should be viewed as one of the fundamental requirements for accession to the European Union, together with the introduction of excise duties on mineral oils, tobacco products and alcoholic beverages. At the same time, Member States retain the freedom to introduce excise duties on other products where justified by fiscal, economic, environmental or other considerations, provided that such measures do not entail additional formalities in connection with the cross-border movement of such goods or result in increased administrative costs. In the field of direct taxation, recognising that this remains primarily a matter within the competence of individual States, a number of recommendations have been adopted with the aim of avoiding double taxation in relation to the taxation of personal income and corporate profits.

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Uticaj evropskih integracia na poreski sistem zemalja članica Evropske Unije

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Rezime: O uređenju poreskog sistema i definisanju poreske politike, odlučuje svaka država na svoj način, zavisno od svih bitnih faktora koji čine obilježje te države. Međutim, na jedinstvenom, unutrašnjem tržištu Evropske unije, zemlje-članice treba da se kreću u približno istim pravcima u pogledu poreskih politika koje vode, iz razloga što aktivnosti i mjere koje preduzme jedna zemlja mogu imati uticaja u susjednim i drugim zemljama. Evropska unija, u tom smislu, ima samo pomoćnu ulogu, i njen cilj nije da „standaridizuje" nacionalne sisteme poreza, već da osigura da oni budu kompatibilni ne samo jedni sa drugima, već i sa ciljevima postavljenim u Ugovoru o osnivanju Evropske zajednice. S obzirom da porezi sa aspekta predmeta oporezivanja predstavljaju barijeru za ostvarivanje osnovnih principa slobodne trgovine i osnovnih elemenata unutrašnjeg tržišta, nametnula se potreba za harmonizacijom (usklađivanjem) određenih poreskih zakona, država koje su članice Evropske Unije, ali i država koje su opredjeljene za to članstvo.

Ključne riječi: unutrašnje tržište, poreska konkurencija, pravo Evropske unije