A BAD MONTH FOR LUXEMBOURG

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Luxembourg made front-page news last month with the leak of hundreds of documents that had been signed when current European Commission President, Jean-Claude Juncker, was prime minister and finance minister of Luxembourg. The leak, exposed by the International Consortium of Investigative Journalists ("I.C.I.J."), revealed confidential agreements approved by Luxembourg authorities that provided tax relief to more than 340 global companies.

The leaked documents implicated not only private companies but also revealed that the Canadian government received a tax ruling for its Public Sector Pension Investment Board, which manages pensions for all Canadian federal employees. The Canadian Pensions Board issued a statement addressing this ruling and claimed that since it is tax-exempt in Canada its ruling is not tax avoidance as it has "no tax advantage."

The European Union Antitrust Authority is now expected to expand its ongoing illegal state aid probe using the leaked documents in its investigation. A high-level European Commission official said, "We expect to expand our current request for documents…These documents are now available. They are clearly relevant to the ongoing probe, which is a high political priority."

POLITICAL PRESSURE

The leaked documents put Luxembourg in hot water, especially former prime minister and finance minister, Jean-Claude Juncker, who now faces great political pressure to explain his role in the scandal. He is accused of acting to enrich his country at the expense of its European partners. His actions are purported to have been in defiance of the E.U. spirit, which he hopes to represent as the new Commission President.

Juncker had only been in office for a few days when the I.C.I.J. released the leaked documents. The leak gave anti-E.U. political parties the opportunity to use the motion of censure to demand his resignation. However, Juncker survived the November 27 no-confidence vote and remains in office. While speaking to Parliament, President Junker assured the E.U. that he would not interfere with the ongoing E.U. illegal state aid investigation into the tax schemes of Luxembourg, Ireland, and the Netherlands for tax rulings made with large multinational companies like Ikea, Apple, and Starbucks.

TAX HARMONIZATION

Speaking in front of Parliament, President Juncker insisted that that the Luxembourg tax rulings were legal and that 22 other E.U. member states have similar arrangements with multinational companies. He agreed that there was probably some tax avoidance in Luxembourg, just as in any other E.U. country, and blamed the problem on insufficient tax harmonization in the E.U. President Juncker promised both Parliament and the G-20 summit that he intends to fight tax evasion and tax avoidance by making it mandatory for E.U. member states to inform other member states of their tax rulings with multinational companies and renewing efforts to garner support from E.U. member states for a common consolidated corporate tax base system. On November 12, Juncker told reporters that, "At the moment, there are so many divergences between national legislation – between the definition of what income is taxable – it is possible to engage in a form of fiscal engineering." A harmonized system might reach a dead end, as it requires the support of all 28 member states. Addressing the harmonized tax system following the scandal, Luxembourg's current Prime Minister Xavier Bettel said in an interview with a Belgian newspaper that he will not support proposals to move the E.U. towards one tax system with uniform rates.

A long time has passed since the first discussions of a unified tax system started in Europe, but it is not surprising that the recent Luxembourg scandal has initiated renewed interest in the subject – if not for other reasons, then at least as an attempt to divert attention from Juncker's role in the controversy.

However, information exchange is not the only ongoing measure to combat tax evasion and tax avoidance; the Base Erosion and Profit Shifting ("B.E.P.S.") recommendations of the O.E.C.D. will also assist in furthering these efforts. Shortly after the leak was exposed, the O.E.C.D. Secretary-General spoke at a forum in Paris hosted by the Académie Diplomatique Internationale and the International New York Times. He referred to the Luxembourg scandal as a "wake-up call" to countries, saying that new tax rules are needed to fight B.E.P.S. by multinational companies and tax evasion by individuals. He noted, however, that in order to get smaller countries like Luxembourg to "play ball by the rules," big countries like the U.K. and the U.S. will also have to end practices that contribute to tax avoidance.

WHAT'S NEXT

At the E.U. level, the current scandal provides much-needed information in the investigation into the Luxembourg's taxation of intellectual property, which was hindered by two challenges filed by the state at the E.U. General Court in April against a request for information on tax rulings. This investigation continues and will likely be broadened.

On a wider scale, the action plan produced by the O.E.C.D. to combat B.E.P.S. calls for a new global tax system. The plan will close gaps in current rules and standards that allow some multinational companies, in particular big internet companies and those that utilize primarily intangible assets, to achieve low effective tax rates by shifting profits to low-tax jurisdictions. It is hoped that this plan, together with an automatic exchange of information, will resolve the existing issue of tax evasion and tax avoidance.