EU Braces for Trump 2.0

by Elodie Lamer and Sophie Petitjean

The EU is better prepared to respond to President-elect Donald Trump's tax and tariff threats than it was in 2016, but the bloc is still bracing for four challenging years.

There was no hangover effect when EU ambassadors met November 6 to the fresh news that Trump had been reelected president of the United States, according to an EU diplomat.

What might have come as a surprise in 2016, when Trump beat Democrat Hillary Clinton, was anticipated this time, with the formation of a dedicated task force to ensure that the EU will be assertive when Trump decides to hit the bloc with tariffs, according to media reports. The feeling among ambassadors is that the EU is "a respectable lady in her 70s and no longer the fragile little sister of the United States," the diplomat said.

"Undoubtedly, it remains advantageous for the EU and U.S. to work together rather than against each other," Maroš Šefčovič, commissioner-designate for trade and economic security, interinstitutional relations and transparency, told the European Parliament November 4. He said he would put forward an offer of cooperation but would be ready to stand up for the EU's interests.

One of the most pressing issues for international tax cooperation might be pillar 2. For now, the United States' global intangible low-taxed income regime is not equivalent to pillar 2, as it is not calculated on a jurisdiction-by-jurisdiction basis (jurisdictional blending). EU countries would rather avoid applying the undertaxed profits rule under pillar 2 to U.S companies but might infringe the EU directive if they don't.

Former OECD tax director Pascal Saint-Amans told *Tax Notes* the United States will likely put pressure on Europe not to apply the UTPR, but the EU's response might vary depending on the level of trade tensions the new Trump presidency will impose. "If there are a lot of tariffs imposed, I don't see the Europeans bow on this issue," Saint-Amans said.

The DST Dilemma

Pillar 1, on the other hand, was already frozen under the Biden administration, and "I don't see a new Trump administration try to find two-thirds of the Senate to ratify it," Saint-Amans said. But the United States will still put pressure on countries not to apply unilateral digital services taxes under threat of retaliatory tariffs and other measures, he said.

If Europe expects to negotiate peace in a future trade war with the United States, it may as well implement DSTs now, Saint-Amans said. "When you prepare to negotiate peace, you try to conquer as many territories as possible," he said.

Saint-Amans noted that U.S. tech giants are still on Europeans' radar, as shown by the recent raids of Netflix's offices in Paris and Amsterdam as part of a tax fraud investigation.

Trump recently said Apple CEO Tim Cook called him to complain about a decision by the EU's Court of Justice ordering Apple to claw back more than €13 billion in illegal state aid to Ireland. Trump reportedly responded that, once elected, he will not let the EU "take advantage of our companies."

Members of the OECD's inclusive framework on base erosion and profit shifting have said in the past that the constant threat of unilateral DSTs created both tensions and momentum to move forward on the OECD's two-pillar global tax reform plan. The problem with the EU's DST threat in the first Trump era was the reluctance of certain countries, including Germany, to move unilaterally as a bloc.

The EU Council legal service also set a cat among the pigeons in 2018, saying the European Commission's proposal for a DST imposed as a turnover tax could not be seen as an indirect tax, as it "consists of a tax levied on the revenue of the taxable person in such a way that it is not certain that it will be ultimately borne by the final consumer."

Following that legal opinion, countries including the Czech Republic, Finland, Ireland, and Sweden warned that a DST could be incompatible with the bloc's international obligations. The commission initially chose to propose a turnover tax because it wasn't possible to tax profits without renegotiating EU member states' tax treaties with non-EU countries. A new

DST might run into the same legal issue, and an EU tax on consumers would not be very popular.

An Unwelcome 'Wake-Up Call'

In his book "Paradis Fiscaux," Saint-Amans said it was "mean Trump" that agreed to start negotiating international taxation reform to keep up with the digitalization of the global economy, while "nice Obama," Trump's predecessor from 2009 through 2016, had refused to do so.

But the accounts of Saint-Amans and former French Finance Minister Bruno Le Maire about the years of negotiations over the two pillars underscore the Trump administration's backtracking on issues agreed to by U.S negotiators. Saint-Amans blamed that on the "disconnection between Trump's ministers and their advisors."

Republican senators' repeated threats to defund the OECD based on the argument that its negotiated tax deals undermine U.S. economic interests is also a cause of concern in the EU, although those threats haven't materialized. Also, it is unlikely that the United States would consider the U.N. a better forum in which to discuss the international tax framework.

Trump's reelection is a "wake-up call to Europe," Sean Bray, director of European policy at the Tax Foundation, said on Linkedin. In addition to the possible death of pillar 1, DST retaliation, UTPR retaliation, retaliation over the carbon border adjustment mechanism, and other types of tariffs, the EU should expect a destabilized neighborhood and increased defense spending, Bray said, as Trump has also threatened in the past not to help protect NATO members in case of a Russian attack.

But even as they faced the prospect of a Trump victory during the last few months, some countries remained reluctant to increase the EU budget or adopt new own resources to finance it — whether for defense needs or other strategic autonomy needs. The stakes are huge for the commission, which in 2025 is scheduled to present its budget for 2028-2035. The commission hasn't yet found a way to repay the €800 billion loan incurred to fund the EU's post-pandemic recovery plan without cutting existing financing programs or raising member states' direct contributions.

Repaying the joint debt to the financial markets could cost up to 15 percent of the EU's annual budget as of 2028 and for the following 30 years, Stéphanie Riso, director general at the European Commission's Directorate General for Budget, estimated at a September 4 Bruegel event.

To that end, the commission in June 2023 proposed three additional own resources: a portion of the revenues from the carbon border adjustment mechanism, a portion of the revenues from the emissions trading system, and a statistical own resource based on companies' profits in different EU member states. But while member states agreed on the rules for the carbon border adjustment mechanism and the emissions trading system, they opposed the idea of using them as an own resource. The statistical own resource was no more successful.

In her political program after the EU elections, Commission President Ursula von der Leyen reiterated her support for "new own resources . . . to ensure sufficient and sustainable financing for our common priorities." In a draft political declaration to be adopted November 8, member states said they are committed to "continue the work towards the introduction of new own resources."

Red Tape Strangling Tax Policy

Trump's reelection could boost the debate on other additional own resources. Saint-Amans said an external tax border — for example, in the area of personal income tax — could be useful. In an interview with Agence Europe October 17, Danuše Nerudova, the new European People's Party rapporteur for the EP on own resources, opposed the idea of a new own resource based on companies' profits. That would push investors to leave Europe for the United States, as Trump has promised to cut international corporate taxes, she said.

"Before the U.S. elections, the Draghi report already emphasized the need for strategic tax policy adjustments to improve competitiveness and increase economic growth, especially compared to the U.S. and China. Trump's election might accelerate that need. Potential reductions in U.S. corporate tax rates may pressure EU countries to lower their own rates, risking a decrease in tax revenue," Gregory Jullien and Roberta Poza Cid of Deloitte told *Tax Notes*.

"Additionally, if Trump successfully convinces businesses to relocate from the EU to the U.S., economic growth of EU Member States and their tax revenues could be further negatively impacted," Jullien and Poza added.

Saint-Amans said he believes the commission's promise to declutter EU tax legislation has a key role to play. The OECD also said it should declutter its BEPs project but has yet to indicate which rules pillar 2 made redundant or useless.

"Avoiding 50 layers of regulation, providing more legal certainty, [and] eliminating double taxation" might improve the EU's competitiveness, Saint-Amans said. The EU is also reviewing its anti-tax-avoidance directive, which transposed BEPS into EU law.

It would be advantageous to be first in the decluttering movement, Saint-Amans said. ■

Unequal Taxation of Dutch Dividends Violates EU Law

by Michael Smith

Requiring nonresident companies to pay dividend withholding tax when resident Dutch companies are essentially exempt violates the EU rules on the free movement of capital, the Court of Justice said.

In a November 7 decision in *XX v. Netherlands*, C-782/22, the Court determined that article 63 of the Treaty on the Functioning of the European Union (the free movement of capital) precludes national legislation that exempts resident state corporations from withholding tax while applying withholding tax to nonresident corporations.

In the Netherlands dividends are generally subject to a 15 percent withholding tax. Resident companies are required to make an advance payment of the dividend tax, which is used to directly offset the corporate tax due at the end of the year and may result in a refund if the tax paid on dividends exceeds the corporate tax liability.

The Court held that resident companies receive preferential treatment by being exempt from dividend withholding tax, finding that it is likely to deter companies from investing in the Netherlands and restricts the free movement of capital.

The unnamed company is a U.K. resident insurance undertaking that invests premiums through unit-linked insurance contracts. Between 2003 and 2010, the company invested in Dutch companies and paid tax on the dividends at the 15 percent rate. However, the company is subject to corporate tax in the United Kingdom and cannot offset the Dutch dividend tax.

The company petitioned the Dutch tax authority for a dividend tax refund but was denied. The company's refund position was rejected in 2020 by the Zeeland District Court as unfounded. The company then appealed to the Court of Appeal, which referred the decision to the Court of Justice of the European Union in December 2022.

The referring court asked whether allowing a resident company to offset its corporate tax liability by the dividend tax paid while simultaneously requiring nonresident companies