Tax Barriers and Cross-Border Workers: Tackling the Fragmentation of the EU Tax Framework

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Presentation for the FISC Subcommittee

Structure of the Presentation

1. Introduction
2. Tax and Worker Mobility in the EU
3. Barriers to Worker Mobility – Compliance Costs of Employers
4. Case Studies
5. Policy Recommendations

Introduction

Background and Aim of the Study

- **Since the COVID-19 pandemic**, the number of cross-border workers, including frontier workers, posted workers, self-employed and remote working individuals, and digital nomads has **increased** significantly.

- All groups of mobile workers are confronted with **diverse** and sometimes **conflicting tax regulations** across EU Member States. This creates **cross-border tax barriers** and contributes to the **fragmentation of the EU's tax framework**.

- The study approaches these challenges from **legal, economic, and business perspectives**, identifying **key problem areas** and exploring **potential solutions** to ensure fair taxation of workers both at the national and EU levels.

- The legal, business, and economic analysis come to the same conclusion: **existing cross-border tax disparities** in the EU make it more **difficult** for individuals to exercise the **right of free movement**.

Tax and Worker Mobility in the EU

Legal Obstacles: a Structural Issue

- In the **absence of an EU tax policy**, secondary EU law on tax matters must meet **strict requirements** and presupposes **impact on the EU internal market**
- Focus on harmonization of corporate tax: **no removal of cross-border disparities on labour**
- **CJEU's interpretation** removed several obstacles imputable to one MS, but not disparities
- Obstacles were already identified in the **2015 EU Commission Report** and in later work, including in the framework of the EESC.
- N**o action on the removal tax obstacles until present in striking contrast with progress of harmonisation of social security law**
- Issues affect the **right to take up a job in another MS and to work from a different MS**

Legal Obstacles: Common Critical Issues

- **Legal uncertainty and ex ante determination of place of exercise of employment**
- **Multilateral issues**: can they be addressed by bilateral treaties and domestic law?
- Tax obstacles on relocation: nudge **EU-wide seamless approach across borders**
- **Full automatic exchange of information** (already in force) might help a more proportionate approach
- **Procedural complexity**
- **Higher exposure to tax audits**

Legal Obstacles: Seen by Category

- **Remote workers**
  - Determination of place of employment and application of Art. 15 of tax treaties
  - Home-office PE
- **Seconded workers**
  - Identification of employer for the application of Art. 15 of bilateral tax treaties
- **High-mobility workers**
  - Place of employment and activity exercised accidentally in multiple countries
- **Frontier workers**
  - Different approaches in bilateral treaties, in some cases with a dedicated clause
- **Digital nomads**
  - Place of employment and activity exercised accidentally in multiple countries
  - Home-office PE

Legal Obstacles: in Year of Relocation

- **Split-year vs full-year rules** affect tax residence
- Overlap between **personal and objective tax nexus**
- Levying of **exit taxes**
- **Procedural complexity**

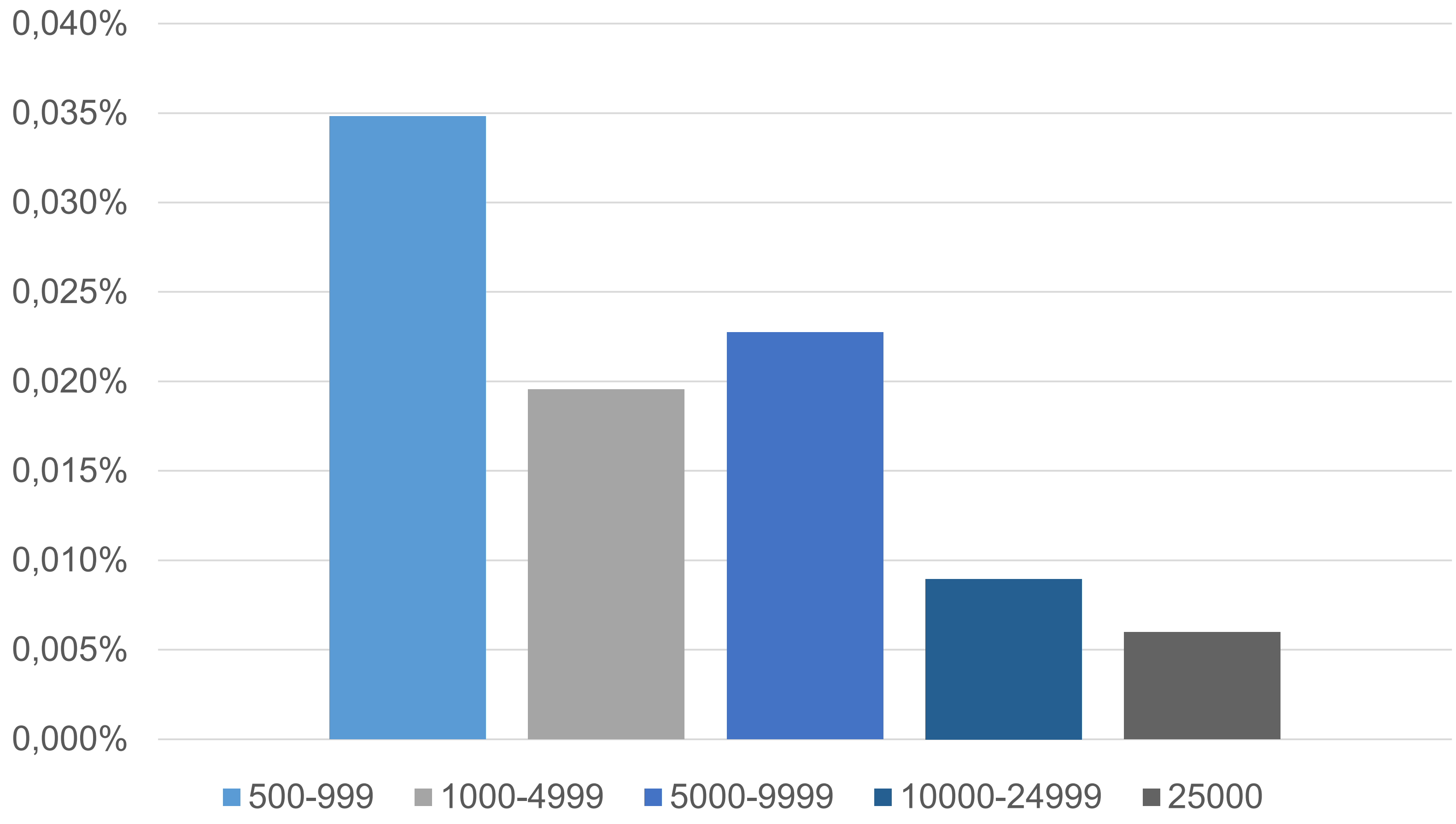
NB – These obstacles affect long- and short-term relocation. They might have multiple effects on the mobility of workers

Barriers to Worker Mobility – Compliance Costs of Employers

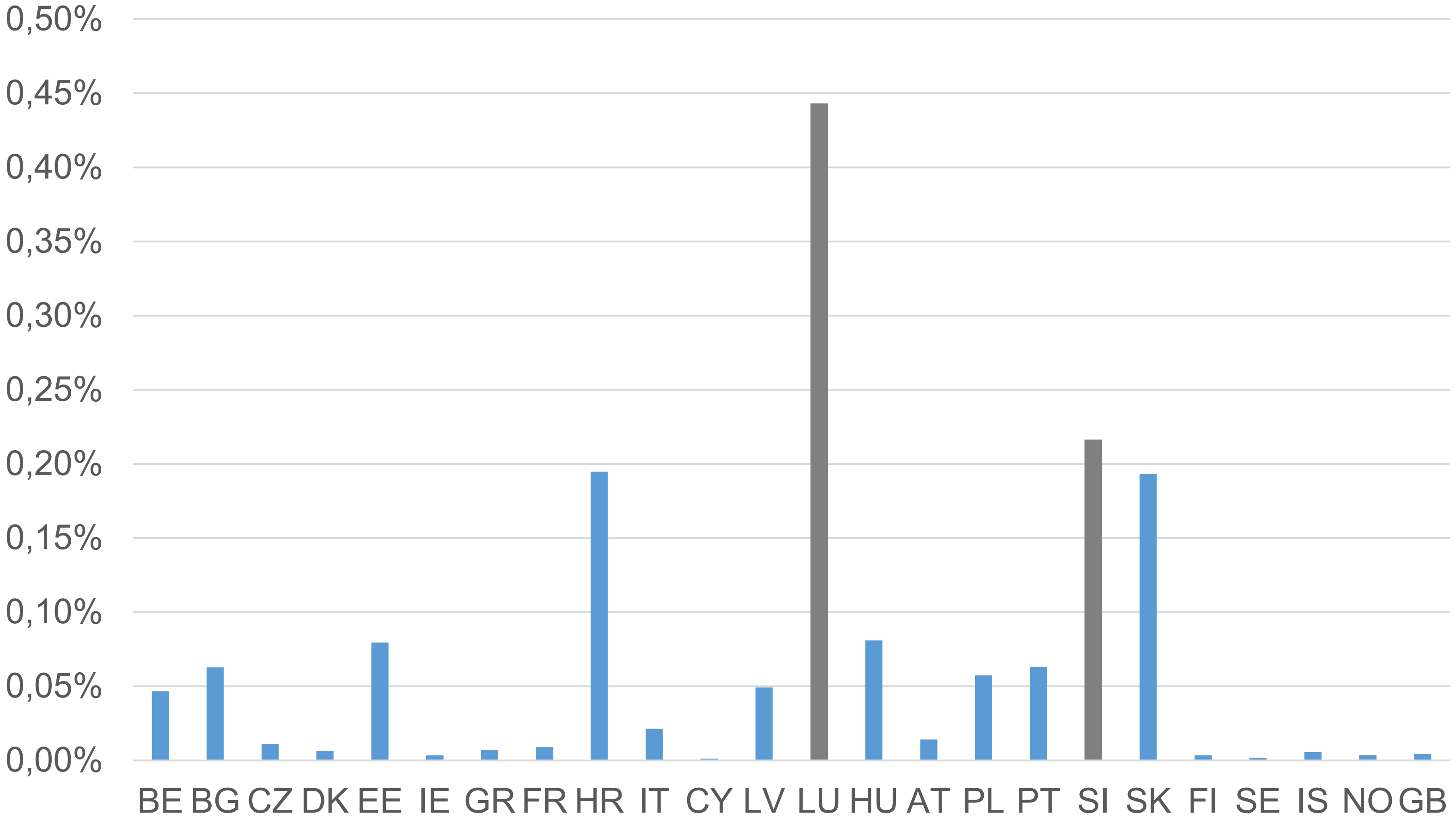
Data and Assumptions

- We use the **PD A1 Statistical database** to estimate the percentage of **posted cross-border workers**.
- To estimate **additional compliance costs (ACC)** incurred by posting workers abroad, we use the difference in costs for **payroll services** performed by an **in-house department** or an **outside expert** .
- In addition, we use **firm-level financial statement data** over the period of **2015-2019** for the **EU/EAA-region** as well as the **United Kingdom** and **Switzerland**.

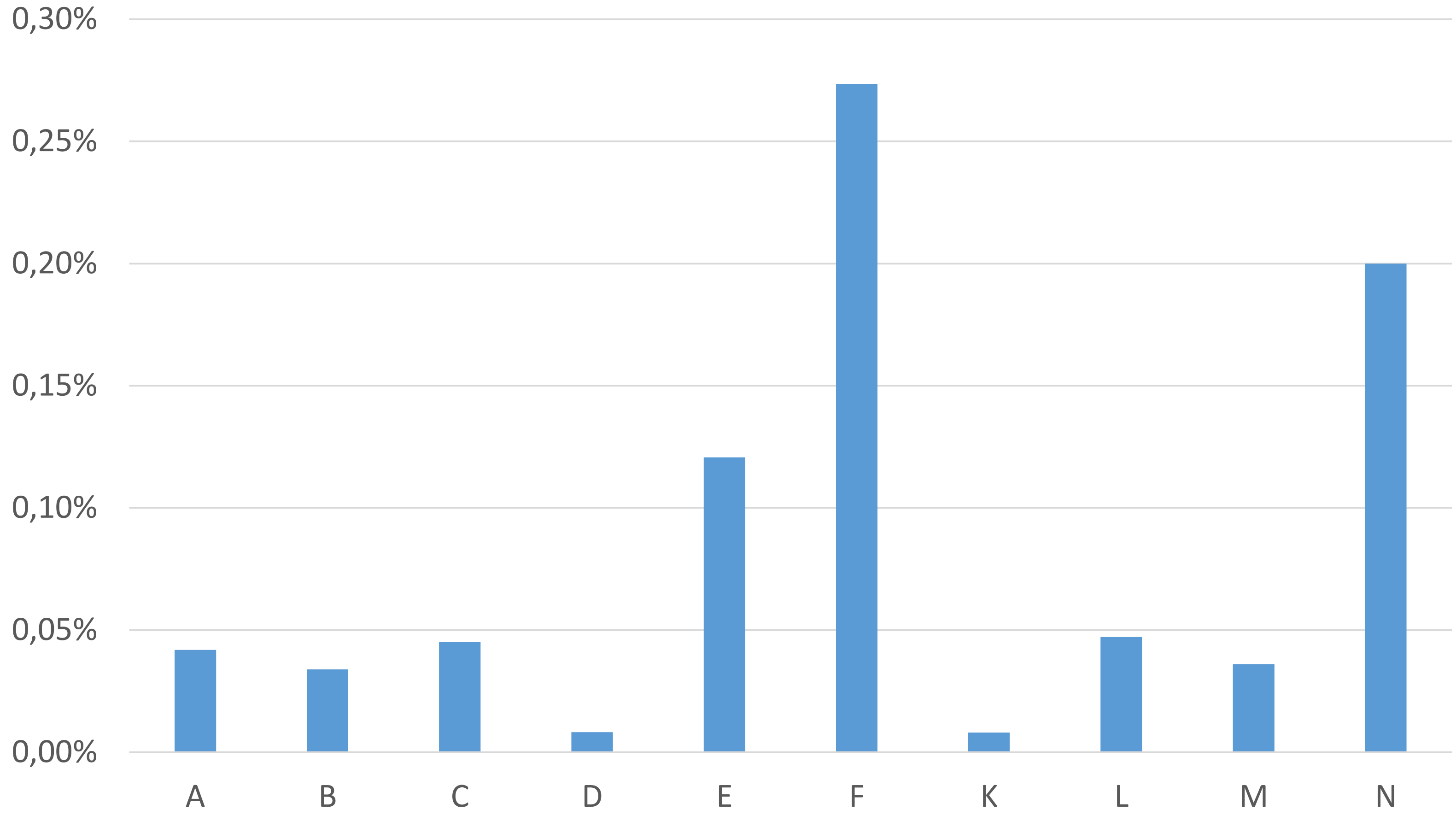
Reduction of Profitability Ratio from ACC by Firm Size



Reduction of Profitability Ratio from ACC by Country

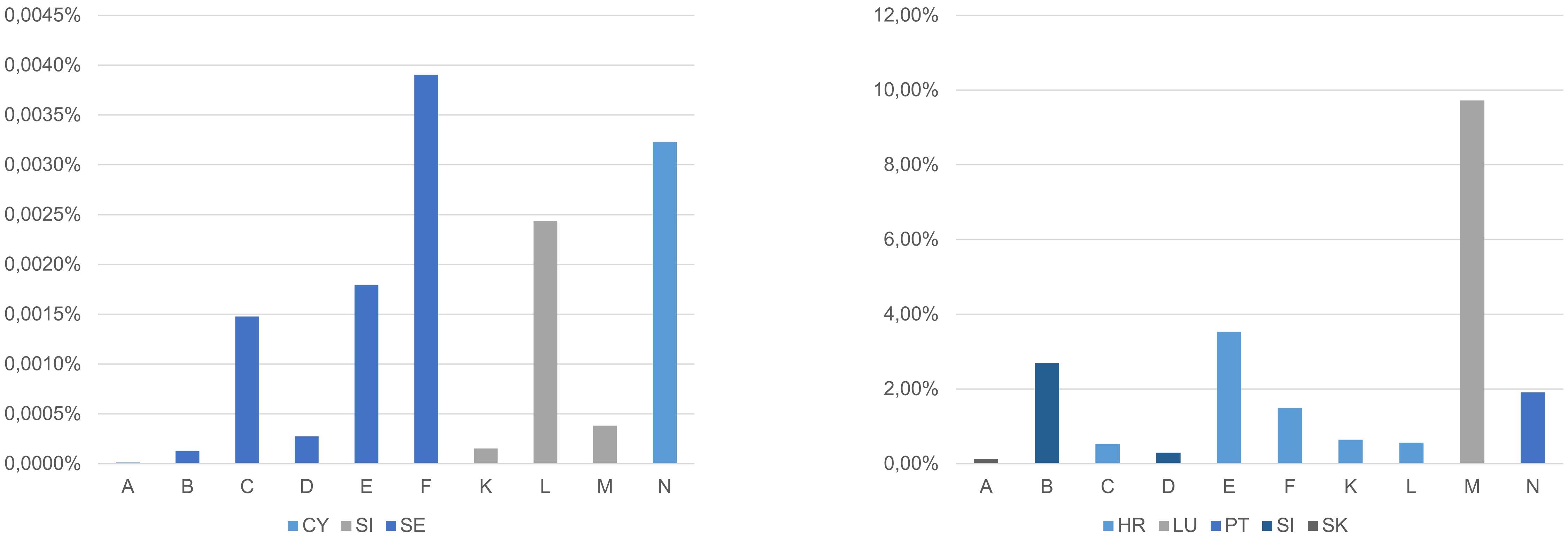


Reduction of Profitability Ratio from ACC by Industry



A(agriculture, forestry and fishing), B (mining and quarrying), C (manufacturing), D (electricity, gas, steam and air conditioning supply), E (water supply, sewerage, waste management and remediation activities), F (construction), K (financial and insurance activities), L (real estate activities), M (professional, scientific and technical activities), N (administrative and support service activities)

Reduction of Profitability Ratio from ACC by Industry & Country



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Results

- **Luxembourg and Slovenia** are the countries that are irrespective of the level of analysis the **most heavily affected**, while **Cyprus and Sweden** are in general the **least affected**.

- The **construction** industry has the **highest reduction** in profitability while the **finance industry** seems mostly **unaffected**.

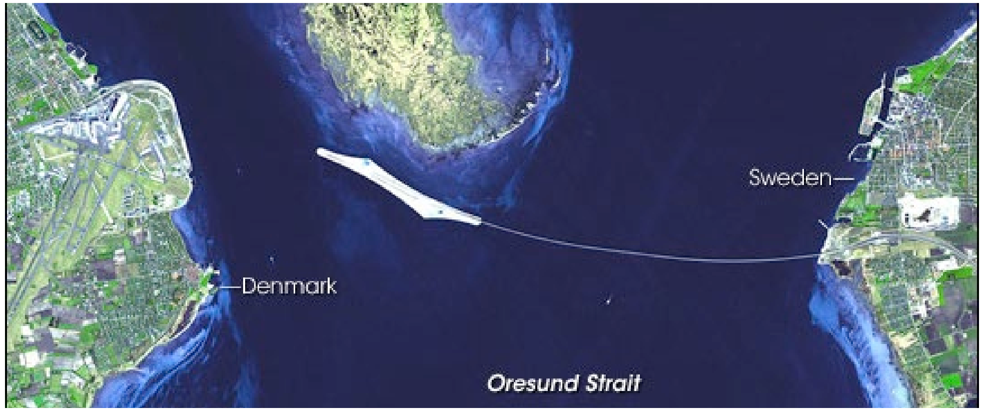
- On a **country-industry level**, **Luxembourg** shows the **highest reduction** in profitability in **professional, scientific and technical activities**. In **Slovenia**, the **mining and quarrying industry** is **most affected**, while **financial, real estate and professional activities** are **least affected**. **Croatia** shows the **highest reduction in profitability in manufacturing, water, construction, finance and real estate industries**. **Sweden** shows the **lowest** ratio in **industries from agriculture, forestry and fishing to construction**.

Case Studies

Case study 1: the Highly-Mobile Worker

- Employee working remotely from a different MS, also working in other MSs, but with very limited physical presence in the MS of employer
- Critical issues:
  - Ex ante identification of place of exercise of employment
  - Higher exposure to unresolved double taxation
  - Multilateral situation
- Critical issues are shared also by remote and seconded workers

Case study 3: Öresund



Case study 3: Öresund

- The Öresund region comprises **eastern Denmark** (notably Copenhagen) and **southern Sweden** (notably Malmö) and is one of the most **integrated cross-border metropolitan regions** in Europe. The **Öresund tax agreement** signed by Sweden and Denmark is designed **specifically** to regulate the **taxation of cross-border workers**.

- If a person works in one country but resides in the other, their **salary** is **taxable** in the **country** where the **work** is normally performed—provided that at least half of the working time (including holidays and sick days) within any **twelve-month period** is spent there.

- A **unique equalization mechanism** has been established to address municipal tax imbalances. When a **resident** of one country **earns** over **DKK 210,000** (2023 price level, indexed) in the other country, the **taxing country** must **transfer** a **standard municipal tax equivalent** to the **residence country.**

Policy Recommendations

Policy Recommendations

GENERAL APPROACH

- Shift focus on positive integration of all law affecting labour mobility
- Bundle tax with social security in a consistent package that secures an effective free movement of workers without obstacles across the borders

SPECIFIC INTERVENTIONS

- Adopting a coordinated application of **"split-year rules"** might be advisable, as it increases tax neutrality, preventing unintended tax advantages and disadvantages.

- A better coordination of **domestic and treaty-based rules** determining tax residence seems to be the first-best solution.

- Whether through common rules of tax harmonisation or coordination, **positive integration** in the context of **exit tax** is necessary to achieve consistent tax treatment between the countries of emigration and immigration.

Policy Recommendations

- The authors of this study invite the EU Parliament to **re-examine** the **1979 EU Commission withdrawn proposal on frontier workers** and support an intervention in this specific domain.

- Internationally mobile workers and their employees face additional **compliance costs** from **various sources. Standardizing** and harmonizing the necessary **disclosure requirements** could diminish these costs.

- The study suggests **carving out intra-EU digital nomads from** the **treatment normally applicable** to remote workers in all cases in which the digital nomad sojourns on a **non-occasional basis in the country of employment**. **In all other cases** of intra-EU digital nomads, it is important to **understand** whether the **personal connection** of the digital nomad to one EU Member State has a **predominant nature** over the presence on the territory of others.

Policy Recommendations

- This study does not recommend a **single solution** to the problems of **posted workers**, but rather **including** them within the **scope** of the required changes applicable to **workers relocating to another EU Member State** and workers exercise their work **across borders without an actual relocation** to a different EU Member State.

- The authors suggests **bundling highly mobile individuals with frontier workers** within the **same form of positive integration**, applying exclusive allocation of taxing powers to the State of residence or a mechanism of fully refundable WHT.

- Since **tax treaties** were designed when remote working was extremely rare, their **clauses on income from employment** are mostly **not fit** to apply to activities not exercised at the business premises.

Thank you for your attention!

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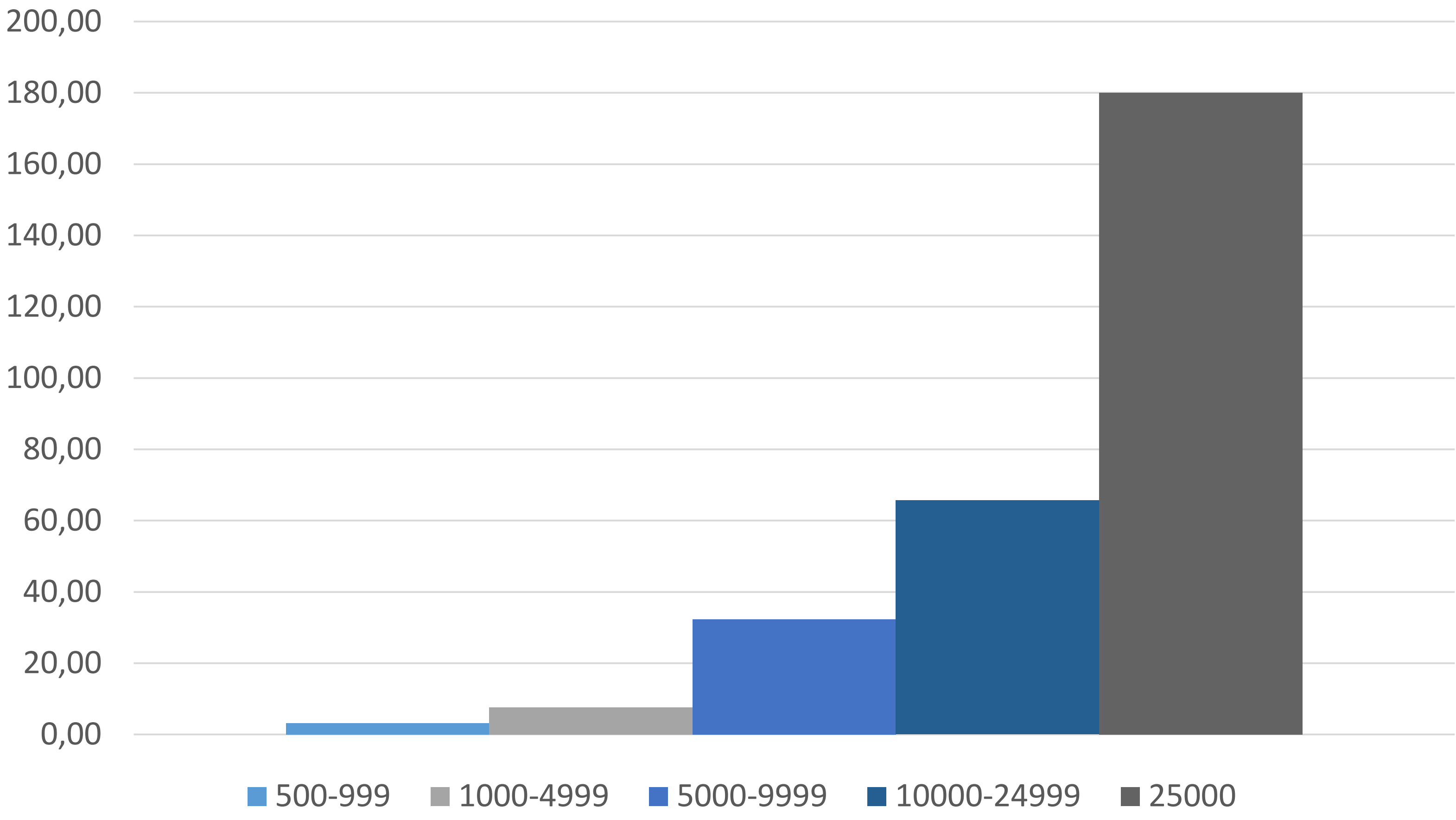
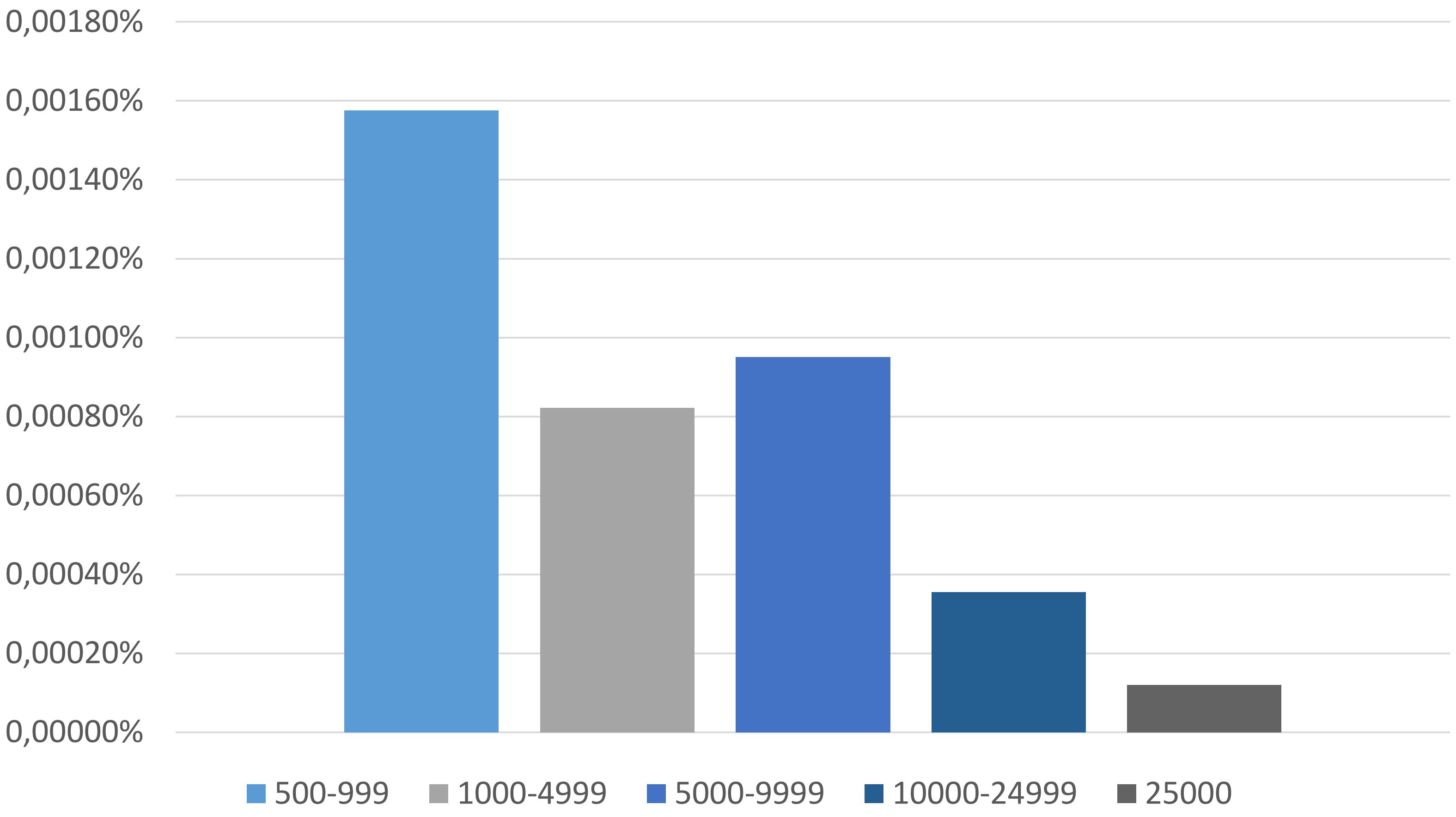
Appendix

Mobile Workers per Firm Size

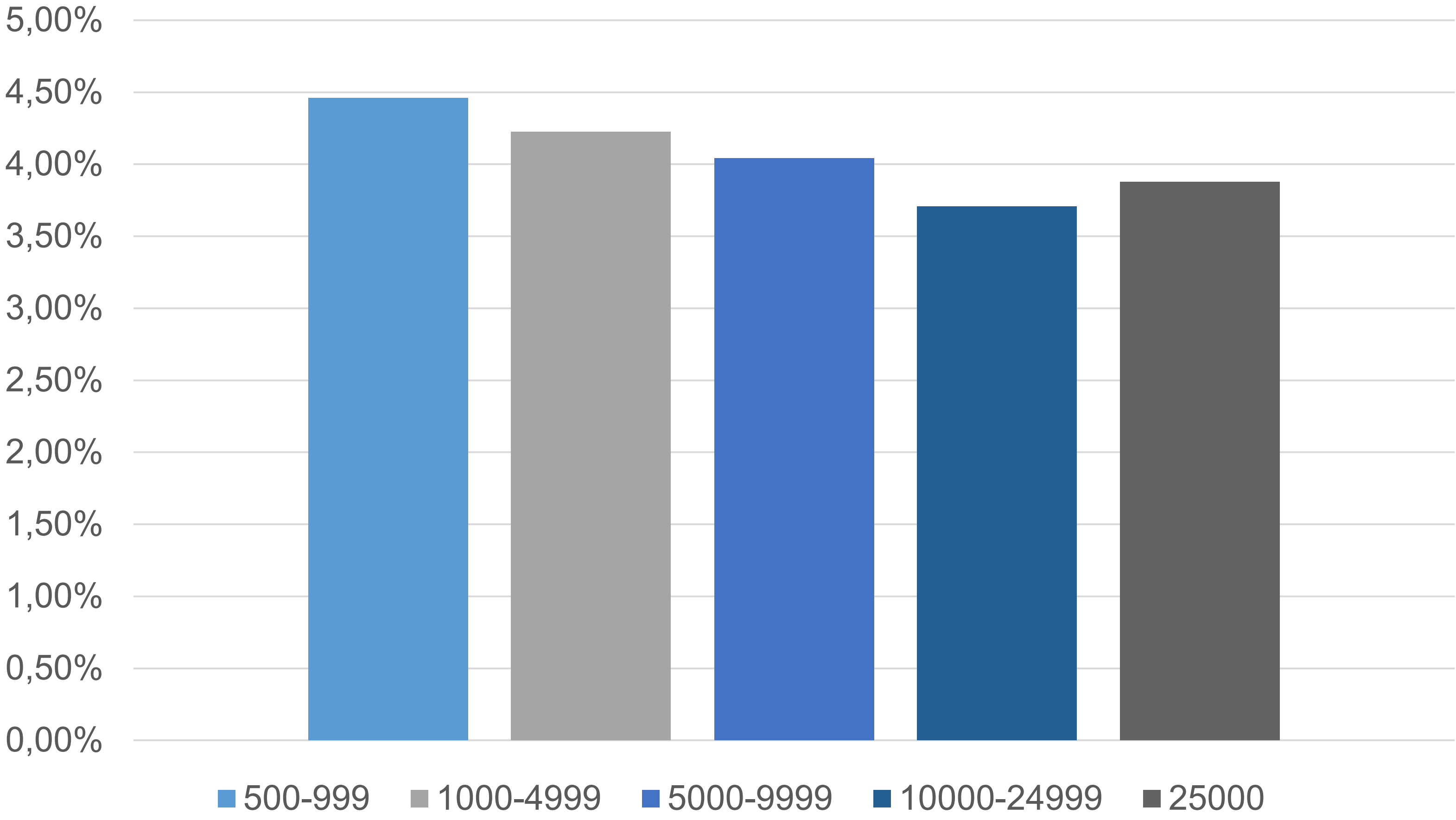


ACC–TO-Ratio per Firm Size

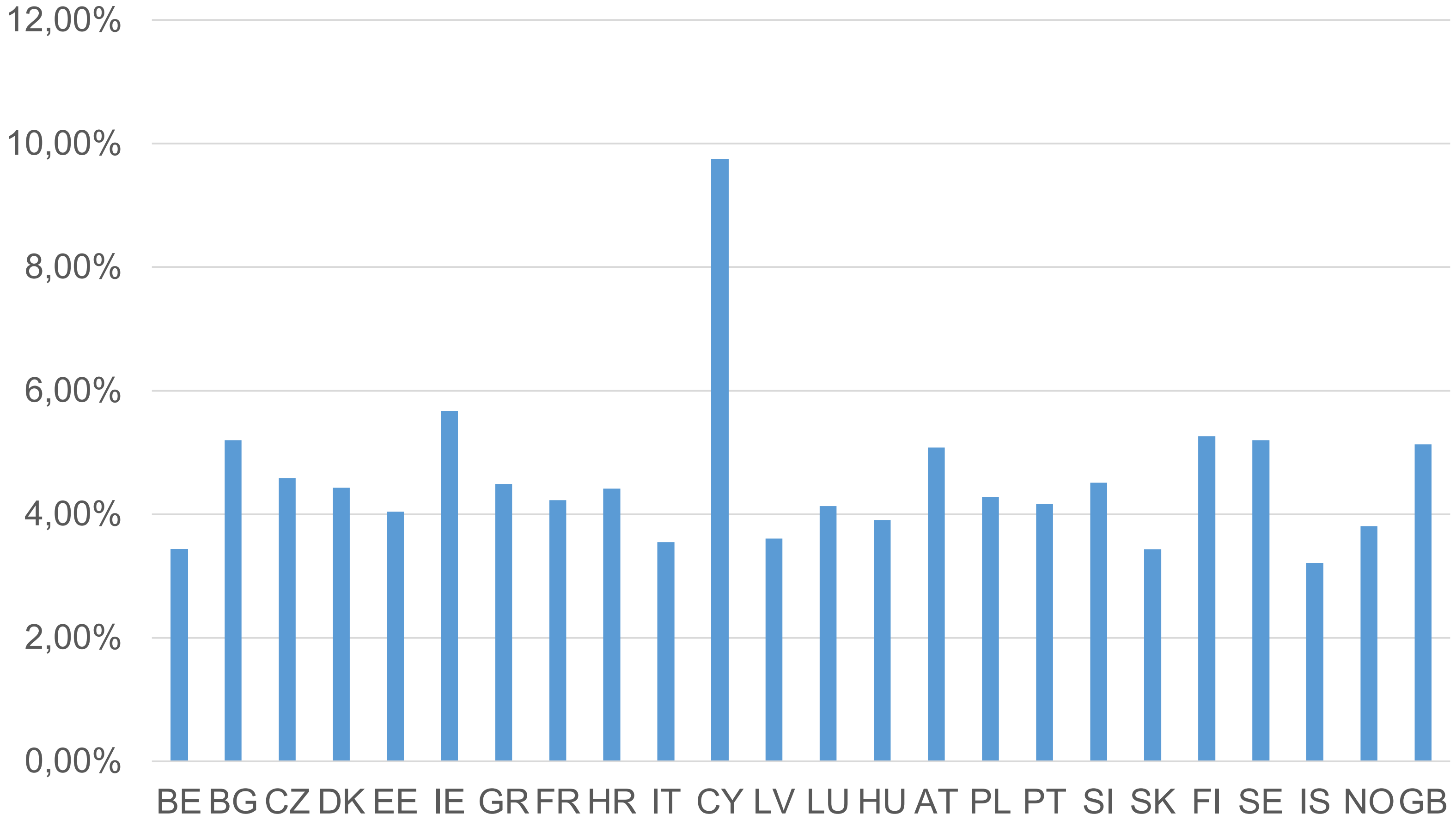


Average Profitability Ratio per Firm Size

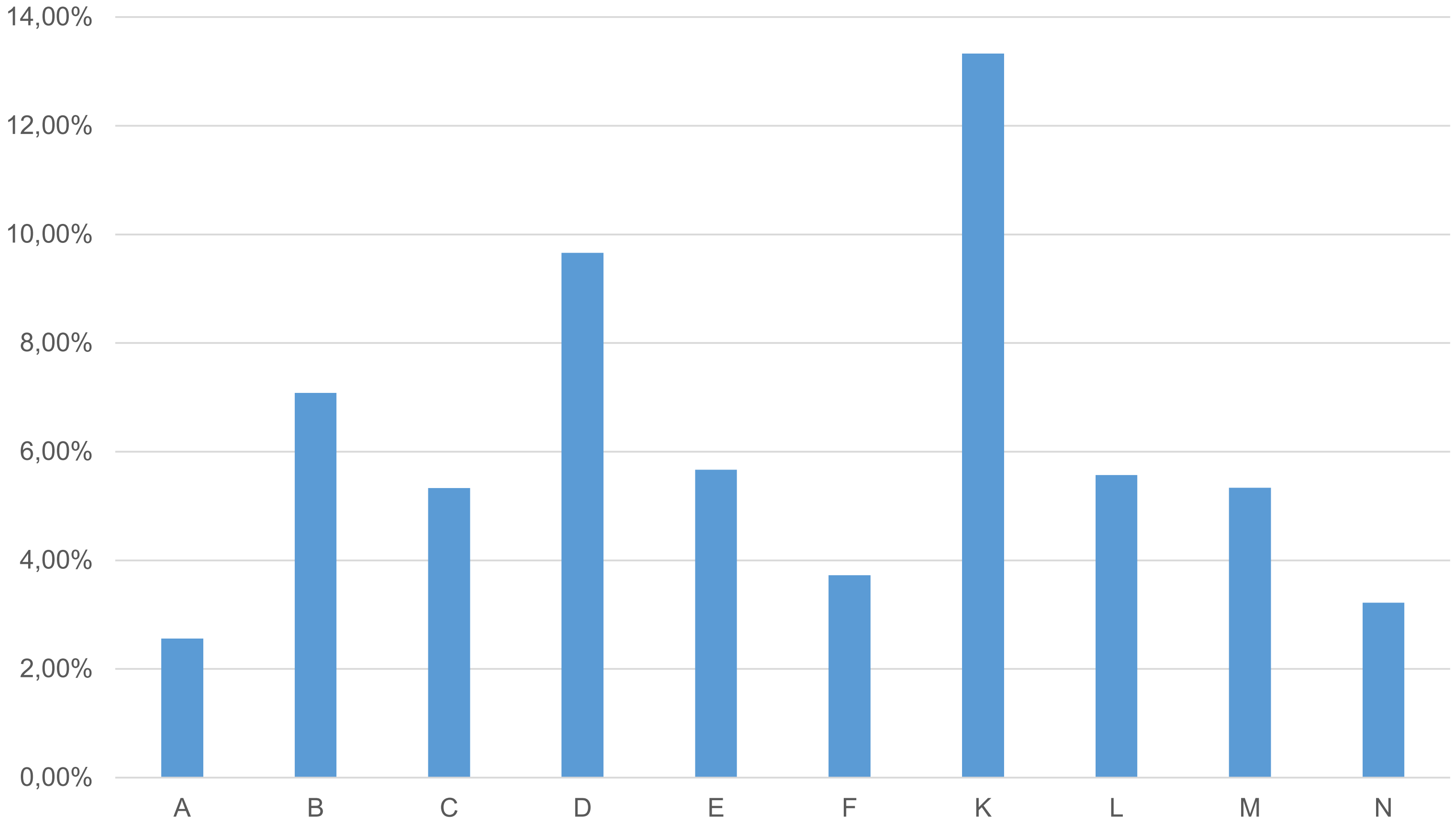
(number of employees)



Average Profitability Ratio by Country



Average Profitability Ratio by Industry



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