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Fair distribution of taxes in transfrontier areas

Potential conflicts and possibilities for compromise

Governance Committee

Rapporteur:[1] Karl Heinz LAMBERTZ, Belgium (R, SOC)

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Summary

Transfrontier working, the free movement of labour across borders, is a vital aspect of European co-operation and integration, all the more so given that a third of Europe's citizens live in border areas.

While progress has been made on many of the obstacles to such co-operation, the lack of equitable distribution of transfrontier worker tax revenues on both sides of the border remains problematic. Disparities in the taxation of cross-border workers can lead to an unequal share of local revenues generated by cross-border flows, creating a winner-loser situation, in which local and regional authorities on one side of the border benefit from this exchange at the expense of their counterparts on the other side.

This report examines the situation in several border areas, making recommendations as to how to ensure a fairer distribution of the tax revenues generated by such cross-border work.

1 L: Chamber of Local Authorities / R: Chamber of Regions
EPP/CCE: European People's Party Group in the Congress
SOC: Socialist Group
ILDG: Independent and Liberal Democrat Group
ECR: European Conservatives and Reformists Group
NR: members not belonging to a political group of the Congress

RESOLUTION 449 (2019) [2]

1. Transfrontier working, the free movement of labour across borders, is a vital aspect of European co-operation and integration, all the more so given that a third of Europe's citizens live in border areas. The Council of Europe, including the Congress, has for many years been a pioneer in developing this co-operation, working to change Europe's internal borders from barriers to bridges, opportunities for co-operation to improve the quality of life for citizens on both sides of the border.

2. But while progress has been made on many of the obstacles to such co-operation, the issue of the equitable distribution of transfrontier worker tax revenues on both sides of the border remains to be solved.

3. While Council of Europe member States generally apply the OECD rule that the transfrontier worker pays tax at the place of work, the growth of transfrontier working in recent years has highlighted the need for this practice to be accompanied by the fair distribution of this revenue, on both sides of the border, to benefit both the place of employment and the place of residence.

4. The European Union has no common policy on this, despite having affirmed the need to establish a common principle on cross-border taxation in a Commission Recommendation as long ago as 1993. In the absence of a common approach, the response to this problem remains the responsibility of the authorities of each country, which has led to a multiplicity of bilateral agreements.

5. In some cases, systems of tax retrocession or financial compensation have been adopted to cover the excess of expenses (such as schools and infrastructure) borne by the place of residence. In other cases, no agreement has been concluded, leaving the local and regional authorities of the places of residence bearing costs much higher than the places of employment.

6. As a result, there are regions in which the financing of public services in border areas is woefully inadequate, as a result of this exclusive collection by the fiscal authority of the country of employment. This can cause serious tensions for the communities concerned and affect their ability to invest because of the budgetary pressure linked to demographic change exacerbated by the labour needs of the neighbouring country.

7. The risk of further aggravation of such unbalanced cross-border development is a challenge for European decision-makers. A line that divides rich and vibrant centres, concentrating jobs and wealth from suburban-dormitories, characterised by the impoverished communities in some regions, is unsustainable in the long run. The unequal distribution of burdens and the benefits of employment can only weaken interregional links on the European continent and undermine territorial cohesion.

8. In this context, it is necessary to deepen and organise the debate on tax policy in cross-border areas, accepting that the place of taxation is less relevant than the need for co-operation and agreement between the authorities concerned, and identifying new solutions to this problem.

9. For this debate to yield results, substantial progress needs to be made to improve the knowledge and understanding of the issue, through extensive research and data gathering, based on common indicators.

10. In view of the above, the Congress,

a. Bearing in mind:

i. the European Outline Convention on Transfrontier Co-operation between Territorial Communities or Authorities (Madrid Convention) of 21 May 1980, and its additional protocols (ETS Nos 106, 159, 169 and 206);

ii. Congress Resolution 363 (2013) on prospects for effective transfrontier co-operation in Europe;

2 Debated and adopted by the Congress on 29 October 2019, 1st sitting (see Document CG37(2019)10, explanatory Memorandum), Rapporteur: Karl Heinz LAMBERTZ, Belgium (R, SOC)

iii. the report of the Foundation for the Economy and Sustainable Development of the Regions of Europe (FEDRE) on "The fair distribution of taxes and charges in cross-border areas" (December 2018) and the seminar it organised in October 2018 in Geneva which gathered stakeholders of the targeted area;

b. concerned about the problems of financing essential public services, including education, kindergartens, social housing and communication infrastructure in certain frontier areas;

c. convinced that stronger relations and partnerships between dynamic centres and areas of residence are important preconditions for the construction of virtuous business cycles, environmental performance, territorial cohesion and social sustainability in the member States of the Council of Europe;

d. convinced of the viability of long-term cross-border strategies based on the sharing of the fruits of labour to develop common infrastructures;

e. concerned about the dynamics of tax competition between Member States and the need to ensure that certain regions and municipalities remain attractive places to live and work;

f. resolved to guarantee the principle of non-discrimination and to avoid double taxation;

g. invites the local and regional authorities of places of residence of transfrontier workers in Council of Europe to:

i. support the technical, scientific or linguistic training of their border populations to enable them to make better use of cross-border job opportunities;

ii. abolish barriers to cross-border mobility;

iii. take into account the evolution of teleworking, which can reduce mobility, by studying the measures that should be taken in order to make it attractive for both employees and companies;

h. Invites the local and regional authorities of places of employment of transfrontier workers in Council of Europe member States to:

i. promote co-development as a common goal, to promote economic growth, and to distribute the resulting tax revenues equitably and to transform them locally into improved quality of life;

ii. contribute to the financing of the local public services used by these workers in their places of residence;

i. Invites national associations to support research in this area, including data collection and the development of common indicators.

RECOMMANDATION 438 (2019)[3]

1. Europe's border regions are the laboratories of European integration. For 40 years, the Council of Europe has been in the forefront of developing this co-operation, changing the perception of Europe's internal borders from one of barriers to one of bridges, opportunities for co-operation that can and do benefit citizens on either side of the border. Against this backdrop, the need to ensure an equitable distribution of transfrontier worker tax revenues on both sides of the border stands out as one of the major challenges to such co-operation.

2. The free movement of labour across borders is one of the strengths of European co-operation, all the more important in the light of the fact that a third of Europe's citizens live in border areas. However, like any integration process, the free movement of labour leads to imbalances, particularly in terms of taxation.

3. Council of Europe member States generally apply the OECD rule that the worker pays tax at the place of work. The growth of cross-border working in recent years has highlighted the need for this principle to be accompanied by one of the fair distribution of this revenue, to the benefit of both the place of employment and the place of residence.

4. The European Union has no common policy on this, despite having underlined the desirability of establishing a common principle on cross-border taxation in a Commission Recommendation in 1993. In the absence of a common approach, the adaptation of legal structures to meet the needs of transfrontier working remains the responsibility of the authorities of each country, which has led to a multiplicity of bilateral agreements.

5. In many cases, systems of tax retrocession or financial compensation have been adopted to cover the excess of expenses (such as schools and infrastructure) borne by the place of residence. In other cases, no agreement has been concluded, leaving the local and regional authorities of the places of residence bearing costs much higher than the places of employment.

6. As a result, there are many situations in which the financing of public services in border areas is woefully inadequate as a result of this exclusive collection by the fiscal authority of the country of employment. This can cause serious tensions for the communities concerned and affect their ability to invest because of the budgetary pressure linked to demographic change exacerbated by the labour needs of the neighbouring country.

7. The risk of further aggravation of such unbalanced cross-border development is a challenge for European decision-makers. A line that divides rich and vibrant centres, concentrating jobs and wealth from suburban-dormitories, characterised by the impoverished communities is unsustainable in the long run. The unequal distribution of burdens and the benefits of employment can only weaken interregional links in the European continent and undermine territorial cohesion.

8. In this context, it is necessary to deepen and organise the debate on tax policy in cross-border areas, knowing that the place of taxation is less relevant than the need for co-operation and agreement between the authorities concerned, and identifying new solutions to this problem.

9. For this debate to yield results, substantial progress needs to be made to improve the knowledge and understanding of the issue, through extensive research and data gathering, based on common indicators.

10. Reconciling taxpayer expectations with the provision of sufficient resources for tax administrations will require a co-ordinated approach to avoid double taxation and allocate taxing rights on both sides of the borders.

3 See footnote 2

11. In view of the above, the Congress,

a. Bearing in mind:

i. the European Outline Convention on Transfrontier Co-operation between Territorial Communities or Authorities (Madrid Convention) of 21 May 1980, and its additional protocols (ETS Nos 106, 159, 169 and 206);

ii. Congress Resolution 363 (2013) on prospects for effective transfrontier co-operation in Europe;

iii. the report of the Foundation for the Economy and Sustainable Development of the Regions of Europe (FEDRE) on "The fair distribution of taxes and charges in cross-border areas" (December 2018) and the seminar it organised in October 2018 in Geneva, which brought together stakeholders of the targeted area;

b. concerned about the problems that local and regional authorities are facing in financing essential public services, including education, kindergartens, social housing and communication infrastructure in certain frontier areas;

c. convinced that stronger relations and partnerships between dynamic centres and areas of residence are important preconditions for the construction of virtuous business cycles, environmental performance, territorial cohesion and social sustainability in the Member Statesof the Council of Europe;

d. convinced of the viability of long-term cross-border strategies based on the sharing of the fruits of labour to develop common infrastructures;

e. concerned about the dynamics of tax competition between some member States and the need to ensure that certain regions and municipalities remain attractive places to live and work;

f. resolved to guarantee the principle of non-discrimination and to avoid double taxation;

g. recommends that the Committee of Ministers resolve to address this issue in its future work programme, by conducting a comprehensive survey of the issues concerned, including the need for systematic data collection and the development of common indicators on the intensity and direction of labour flows, demographic trends, community burdens and the consequences of different tax rates;

h. recommends that the Committee of Ministers invite the governments of its member States to:

i. promote co-development as a common goal, to promote economic growth, and to distribute the resulting tax revenues equitably and to transform them locally into improved quality of life;

ii. encourage the local and regional authorities of places of employment of transfrontier workers to contribute to the financing of the local public services used by these workers in their places of residence;

iii. support the technical, scientific or linguistic training of their border populations to enable them to make better use of cross-border job opportunities;

iv. create the necessary conditions to foster a multilateral tax dialogue in a more collaborative and co-ordinated framework, bringing together all levels of government;

v. standardise the conditions under which the charges are taken into account by the budget of the country benefiting from the labour taxation in favour of the territories of residence of the frontier workers (such as a percentage of the gross wages);

vi. harmonise the principles of burden-sharing between the countries which have borne the initial training costs of frontier employees and the countries which collect the labour tax of these employees, without having contributed to the cost of their training;

vii. harmonise the taxation conditions of frontier pensioners by fixing the place of residence, where the costs of aging are borne, as the place of taxation of pensions;

viii. support the development of Local Groupings of Cross-Border Co-operation (GLCTs) as a means of addressing these issues.

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INTRODUCTION[4]

1. Intergovernmental relations between countries have changed considerably over the last hundred years, evolving from a competitive, conflict-driven relationship into one driven by co-operation. While this change in perspective is best represented by the formation and subsequent expansion of the European Union and the Council of Europe, it is also evident in further agreements between European countries, such as the European Free Trade Agreement and the European Economic Area Agreement.

2. At the core of these agreements is the idea that an increase in economic and social relations between countries can serve to benefit all parties. In that sense, countries have agreed to either remove or reduce the barriers to the development of cross-border economic activities, including the establishment of business and individuals in the countries included in these agreements.

3. This idea is best represented by the 'Four Freedoms', namely the free movement of goods, services, capital and persons, which are laid out in the Treaty of the Functioning of the European Union[5]. These freedoms have also been extended to the relations between EU countries and other members of the European Economic Area, such as Liechtenstein[6]. Similarly, the free movement of persons is also recognised in the relations between the member States of European Union and Switzerland[7]. While free movement as such is a positive development, it raises significant issues concerning the allocation of taxation rights between the countries involved, as well as potential situations of double taxation or double non-taxation for the individuals concerned.

4. We will seek to examine this issue in a holistic manner, focusing on the individual's perspective and from the perspective of the budgetary impact on the countries and regions concerned. We will discuss how the income from cross-border employment should be allocated between countries, taking into consideration the idea that taxpayers should not suffer double taxation and that an increased complexity of the tax system is prejudicial for taxpayers and tax authorities. To do so, the tax treatment of frontier workers[8] in a group of countries will be analysed, namely Belgium, France, Germany, Liechtenstein, Luxembourg, Netherlands and Switzerland. We hope to clarify how the taxation of employment revenue of these individuals is shared between their country of residence and country of employment and identify to eventual pressure points on a country´s budget due to this transfrontier work. Only after such study has been made it will be possible to discuss how to allocate, in a fair manner, the tax proceeds between the countries, while respecting the freedom of movement of individuals, as recognised by the European Union, Liechtenstein and Switzerland.

5. We have chosen to focus on these countries because their border regions are amongst the ones with the highest density of frontier workers in Europe, a phenomenon which has significantly increased over the past 30 years.[9]

I Scope of this report

6. This report is focused on the allocation of taxation rights between countries. Therefore, issues related to social security contributions, as well as the financing of the social security system, even if done via

4 The rapporteur would like to thank the Institute for Transnational and Euregional cross border cooperation and Mobility, University of Maastricht (Dr Fernando SOUZA DE MAN, Prof Anouk BOLLEN-VANDENBOORN and Prof MARJON WEEREPAS), and the FEDRE Foundation and its president Claude HAEGI, former president of the Congress, for their contributions to this report.

5 Articles 45-66, Treaty on the Functioning of the European Union.

6 Article 1(2), European Economic Area Agreement.

7 European Union-Switzerland Bilateral Agreements I of 1999.

8 In this report, "frontier workers" are defined as workers that are resident of one state and work in the other, living in the border region between the states. The definition of "border region" may vary between the states. This work does not focus on workers posted to another state, i.e. workers transferred, for a certain period, to another state for work reasons, because in this case they are indeed living in another state, where they will pay income taxes. The posting issue can raise more issues regarding social security system, which is outside the scope of this work.

9 A recent study showed that Switzerland has 320,000 cross-border workers, comprising 6% of its total workforce, and they come mainly from France, Italy and Germany, https://www.swissinfo.ch/eng/business/cross-border-workers/43795326. Another study shows that in the past 7 years the number of cross-border workers in Switzerland has increased by more than 25%, https://www.thelocal.ch/20170224/cross-border-workers-in-switzerland-rise-by-a-quarter-in-five-years. The same happened in France, where there was an increase of 42% on the number of frontier workers in a period of 12 years ending in 2011, https://www.challenges.fr/economie/les-travailleurs-transfrontaliers-de-plus-en-plus-nombreux-en-france_114799, and in Luxembourg, where from 2016 to 2017 there was an increase of 7.000 frontier workers, http://www.lessentiel.lu/fr/luxembourg/story/pres-de-7-000-frontaliers-de-plus-en-un-an-20302570.

taxes, will not be analysed at this moment. Therefore, we will not discuss which country should collect social security premiums from the employees and which one should pay eventual benefits, such as unemployment payments, dependence insurance and family allowances to the frontier workers.

7. In the same sense, considering the difficulty in effectively measuring the costs municipalities have with frontier workers and the taxes paid by these workers, we will not present an actual framework of the eventual net profits/losses of each country due to the cross-border activities of the frontier workers. These problems are referenced in the report but are not quantified.

8. Ultimately, the allocation of tax revenues within a country is an issue of domestic policy, in some cases even a constitutional matter, so it is for each country, considering its own laws and objectives, to determine how much of the tax income collected should stay with the national or federal government and how much should be forwarded to regional and local governments. In this report this issue will not be analysed, rather the focus will be on looking for a better balance between the collection of tax revenue by national governments, so they can finance the expenses necessary to their functioning and for fostering the economic activities of individuals, and the avoidance of double taxation on the income earned by individuals abroad.

9. Nevertheless, to find balanced and sustainable solutions, these three aspects need to be considered before drawing conclusions and formulating concrete proposals in terms of a distribution of taxation income and sharing costs.

II The issue at hand

10. The act of levying taxes is intrinsic to the sovereignty principle. This is the reason why each jurisdiction tends to exert tax authority over both those individuals residing in as well as those individuals engaged in economic activity in its territory. In the case that an individual is working/developing one economic activity solely in the place in which (s)he is residing, there is only one authority which would levy taxes over his income. Nonetheless, this clear-cut situation is becoming less common, especially in highly integrated regions such as Europe.

11. Nowadays, it is not uncommon for an individual to make use of his freedom of movement to engage in an economic activity in a country different from the one in which (s)he resides. This raises the issue of which country will be entitled to tax this individual’s income. On this matter, there are two leading principles in use worldwide:(i) the residence principle and (ii) the source principle.

12. The residence principle is based on the idea that there is a strong link between the individual and the country in which (s)he resides. There exists a so-called ‘economic allegiance’. In this, the country in which the individual resides is entitled to tax all income earned by this individual, irrespective of the place in which it was earned, as well as to consider the individual´s personal and family circumstances. Furthermore, countries also justify residence taxation based on: (i) benefits that the country grants to residents; (ii) a manner of guaranteeing equal treatment between residents who earn income in the home country and those who earn income abroad. If the income earned abroad is not taxed at home, these individuals would have an incentive and be better off by earning income abroad; (iii) a way of guaranteeing the progressivity of their tax system, i.e. individuals that earn more income need to be held accountable for more taxes.

13. The source principle investigates the issue from the perspective of the country in which the economic activity takes place. Irrespective of where an individual resides, (s)he will pay income tax in the country in which (s)he earns the income. Proponents of this principle of taxation claim that the connection the individual has with the country where (s)he earns such income is stronger than the connection (s)he has with the country of residence. They also claim that source countries also grant benefits to individuals residing abroad (such as access to its domestic market) and equity should be viewed from the perspective of the source country, as irrespective of whether individuals are residents or not; they are competing for the market of the source country, so it would make more sense to tax all individuals engaged in economic activities in the same way.

14. Caught between these arguments, an individual may be held liable for paying taxes in both countries, which can considerably hamper his/her financial position and acts as a disincentive on conducting economic activity abroad.[10] This is an outcome which is certainly not in line with the principle

10 In this case there is a juridical double taxation, since the same individual is subject to tax over the same income.

of free movement of workers widely adopted in Europe. In that sense, individuals should not be subject to double taxation of their income.

15. However, while the lack of double taxation is certainly positive for an individual, it has a great risk, as it may deny a jurisdiction its right to tax either its residents or individuals engaging in economic activities in its territory. The issue becomes even more troublesome in cases where countries are organised in a confederative manner. In this case, the problem can arise as to which federative level is entitled to tax this income (city, state or region).

16. Regarding specifically the issue of cross-border workers, this has been subject to discussion in Europe for a long time. However, apart from specific decisions from the European Court of Justice, no common ground has been found. In that sense, the European Commission drafted a recommendation in 1993 stating that member States of the European Union should have a unified system for the taxation of cross-border workers, guaranteeing that non-residents receive the same tax treatment as residents, if at least 75% of their income was earned in the source state.[11]

17. Even though the recommendation did not entail the drafting of EU legislation, the decision taken by the Court of Justice in the SCHUMACKER case states exactly what was recommended by the European Commission, namely that, when non-residents receive their income entirely or almost exclusively from a country, non-residents should not have a higher tax burden than a resident of this member country.[12] Consequently, the EU member States have introduced in their domestic law rules that deal with the taxation of cross-border workers.

18. In that respect, it is important to note that the difference in treatment may stem both from different tax rates, and from different tax bases. Countries may have different approaches regarding the concession of deductions, credits and allowances, which are a matter of domestic law. The consequence of this being that individuals and companies developing the same activity in the same state may be subject to a different tax burden based solely on the fact that they are resident in different places. In the same sense, the individual might be worse off while developing a cross-border activity because (s)he may not have earned enough income in his/her country of residence. The country of residence may not therefore be able to take the individual's personal circumstances in consideration. A different treatment may also stem because of the nationality of the individual, as seen in the GILLY case.[13]

19. Even if a country intends to avoid this different treatment, there is no guarantee that a common tax base will be achieved, since countries may arrive at diverse calculations of the taxable base since they calculate the taxable base in a different manner.

20. The European Parliament drafted a working paper in 1997 dealing with the topic and the European Commission drafted another recommendation regarding the hindrance of double taxation in Europe.[14] Nonetheless, there is still no unified policy, either in the Council of Europe or the European Union concerning the tax treatment of cross-border workers. There is not even a common definition of a cross-border worker.

21. In the absence of a uniform approach, it is left to national governments (and local authorities) to deal with this issue, based on international agreements, which ultimately lead to different (sometimes conflicting) approaches. On that matter, a balance needs to be struck between the freedom of movement of individuals, their right to work in a country in which they do not reside and the right of national and regional governments and municipalities to collect income earned by their residents as a means to support the provision of services like health, education and possibly even transport.

22. In the coming sections the current situation regarding the most fluid cross-border regions in Europe will be detailed, taking into consideration the positions of the countries involved as outbound providers of frontier workers (individuals live in the state, but work abroad) and inbound recipients of frontier workers (individuals live abroad, but work in the state).

11 European Commission, Commission Recommendation 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. (94/79/EC).
12 Finanzamt Koeln-Altstadt v. SCHUMACKER, ECJ 14 February 1995, C-279/93.
13 GILLY vs. Directeur de Services Fiscaux du Bas-Rhin, ECJ 12 May 1998, C-336/96.
14 European Parliament, Frontier Workers in the European Union, Working Paper, Social Affairs Series, W16A. European Commission, Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee, Double Taxation in the Single Market, document COM (2011) 712 final.

III Belgium

23. For the purpose of this report, attention will be paid to the frontier workers in the border regions of Belgium with France, Germany, Luxembourg and The Netherlands.

1. Frontier workers on the Belgian-French border

24. According to recent data, in 2017 there were 36,524 French residents working in the Belgian side of the border, while there were 7,734 Belgian residents working in France.[15] Thus, it is clear that there is a great imbalance in the flow of employees cross-border, which means that, depending on the allocation of taxation rights established by the countries concerned, one of them will most likely spend more on cross-border workers than it will collect in income from them.

25. According to Article 11 of the Double Tax Convention signed between Belgium and France, as a general rule the remuneration earned by frontier workers shall be taxed exclusively in the country in which the economic activity is exercised, save if they are in the country of employment for less than 183 days, the remuneration is paid by an employer located in their country of residence and is not borne by a Permanent Establishment (PE) or fixed base which the employer has in the working country. Upon fulfilment of these three conditions, taxation should occur exclusively at the country of residence of the employee.[16]

26. Notwithstanding the rules prescribed in Article 11, the countries also agreed on special rules for frontier workers. In that sense, frontier workers should be taxed exclusively at their country of residence if they have a permanent home therein.[17] Furthermore, the frontier zone was considered to include all municipalities at the border as well the ones in a radius of 20 kilometres from the border.[18]

27. After its amendment in 2009, this rule prescribes that, as from January 2007, Belgian residents working in France are under the scope of the general rule of Article 11, i.e. exclusive taxation in France unless the taxpayer fulfils the conditions of Article 11(2) of the Belgium-France Double Tax Convention, case in which Belgium would have exclusive taxation rights over the income of these individuals.[19]

28. For French residents who have a permanent home in France on 31 December 2011 and are working in Belgium, their remuneration shall, for a period of 22 years (starting in January 2012), be taxed exclusively in France, provided that they maintain their permanent home in the French border region, continue to work in the Belgian border region and are not absent from the Belgian border region while performing their work, for more than 30 days per calendar year.[20]

29. In case these specific provisions are not fulfilled, the French resident working in the Belgian Frontier zone will be subject to the general rules of Article 11 of the Double Tax Convention signed between Belgium and France, just like Belgian residents working in France.

30. The prescription of exclusive taxation rights to one of the countries concerned is administratively efficient, since it avoids discussions on the amount of credit which the employee would receive in his/her country of residence due to the taxes paid in the country of employment. Nonetheless, the system contains an inherent flaw; while easy to comply with, it ignores that the national governments/municipalities involved are bearing expenses regarding the frontier workers, for example the municipality will still provide for health benefits and/or education to the frontier worker and his family, but the limitation on the taxation rights of these national governments/municipalities will seriously hamper their budget.

31. Using the data collected as an example, despite the considerable number of French residents which have access to public services in France, their salary will, as a rule, be taxed exclusively in Belgium, so the French state and municipalities will, most likely, experience a disbalance and shortcoming in the funding of their public expenses.

32. However, the change from taxation in the resident state to taxation in the country of work has not led to tax compensation for the Belgian municipalities.

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15 Rijksinstituut voor ziekte en invaliditeitsverzekering, available at <https://www.riziv.fgov.be/SiteCollectionDocuments/statistieken_grensarbeiders_2017.pdf>
16 Article 11, Double Tax Convention France- Belgium
17 Additional Protocol on Frontier Workers, Article 1.
18 Additional Protocol on Frontier Workers, Article 2.
19 Additional Protocol on Frontier Workers, Article 3.
20 Additional Protocol on Frontier Workers, Article 5.

2. Frontier workers on the Belgian-German border

33. The flow of frontier workers between the Belgian-German border is pale in comparison with the Belgian-French border, with recent data showing that in 2017 there were 1,182 German frontier workers working in Belgium and 6,260 Belgian frontier workers working in Germany.[21] Unsurprisingly, there are no special rules between the countries regarding the taxation of frontier workers.[22]

34. Consequently, frontier workers are subject to the general rule of Article 15, which is in line with the OECD Model Tax Convention. Hence, remuneration derived by a resident of a contracting state is taxed exclusively in his country of residence, unless the activity is developed in the source country[23].

35. Even if the activity is developed at the source country, taxation rights may be allocated exclusively to the country of residence of the employee, if (s)he is not exercising his/her employment in the source country for more than 183 days, the remuneration is neither paid by or on behalf of an employer who is a resident of the working state nor borne by a permanent establishment or a fixed base which the employer has in the source state.[24] In such a situation, in which there is not a considerable number of frontier workers involved (less than 7,500 people when considering the influx in both countries), the allocation of the taxation rights between countries is more balanced, since both countries will be entitled to tax the income earned by frontier workers. However, it must be recognised that since most of the frontier workers are resident in Belgium, this State will ultimately benefit more from the taxation rights stemming from the work done by frontier workers (except in case the conditions of Article 15(2) are fulfilled).

36. Local authorities in Belgium levy a municipal tax based on the logic of additional percentages. This is linked to the income tax, of which it represents a percentage that it is for the local authorities to determine (in general, this percentage is between 6% and 8%).

37. A compensation system has therefore been put in place. The municipalities of residence of the frontier workers, apart from any taxation of income, may collect directly from these workers a portion of local taxes calculated on the hypothetical tax corresponding to the income which they now declare in Germany. In return, their tax in Germany is reduced by a flat rate of 8%.

3. Frontier workers on the Belgian-Luxembourgish border

38. There are few frontier workers in the Belgian-Luxembourgish borders, with a huge imbalance of Belgian residents working in Luxembourg when compared with Luxembourgish residents working in Belgium. In 2017, there were 42,061 Belgian frontier workers in Luxembourg[25] and only 545 Luxembourgish frontier workers in Belgium.[26]

39. The countries did not agree on any special rules for frontier workers, so the general rules of income from employment activities are applied, with shared taxation rights if a resident of a country develops an activity in the other country, except when this resident is performing employment activities at source for less than 183 days per year, payments are not made an employer resident in the country of employment and are not borne by a Permanent Establishment (PE) of the employer therein, case in which taxation rights will be exclusively attributed to the country of residence.[27]

40. Furthermore, a recent amendment to the treaty clarified that the time a resident individual who exercised employment in the other country spends performing employment activities in his country of residence or in a third country shall be deemed an exercise of employment in the country of employment, as long as the activities do not exceed, taken together, 24 days.[28]

21 Rijksinstituut voor ziekte en invaliditeitsverzekering, available at <https://www.riziv.fgov.be/SiteCollectionDocuments/statistieken_grensarbeiders_2017.pdf>
22 Interestingly enough, such a provision was part of the treaty, article 15(3), until a protocol signed in 2002 replaced this provision by one in line with article 15(3) of the OECD Model Tax Convention.
23 Article 15(1), Double Tax Convention Belgium-Germany.
24 Article 15(2), Double Tax Convention Belgium- Germany.
25 Rijksinstituut voor ziekte en invaliditeitsverzekering, available at <https://www.riziv.fgov.be/SiteCollectionDocuments/statistieken_grensarbeiders_2017.pdf>
26 Rijksinstituut voor ziekte en invaliditeitsverzekering, available at <https://www.riziv.fgov.be/SiteCollectionDocuments/statistieken_grensarbeiders_2017.pdf>
27 Article 15, Double Tax Convention Belgium- Luxembourg.
28 Protocol signed on 5 December 2017 amending the Double Tax Convention Belgium- Luxembourg.

41. Thus, the taxation rights over the employment income of frontier workers between Belgium and Luxembourg is also shared between the two countries, which, as mentioned above, is a more reasonable outcome since, irrespective of the time spent in a country, the individuals generate expenses to that country.

42. However, the establishment of a financial compensation system of around 15 million Euro in 2002, readjusted to 30 million Euro in 2018, between Luxembourg and Belgium, aims to ensure the financing of Belgian municipalities of which a significant number of residents exercise a professional activity in the Grand Duchy.

4. Frontier workers on the Belgian-Dutch border

43. The last border analysed from the Belgian perspective for the purpose of this work is the one with the Netherlands. In this case it can be noted that there is a higher inflow of Belgian frontier workers performing employment activities in the Netherlands than the other way around, respectively 32,248 as opposed to 11,757.[29]

44. The Belgium-Netherlands tax treaty also adopts the general rule of Article 15 OECD Model Tax Convention for the allocation of taxation rights between the member States, i.e. shared competence if employment is exercised in the country of employment, save if the conditions of Article 15(2) of the treaty, identical to the ones in the two previous sections are fulfilled. Additionally, there are special compensation arrangements in place for the Dutch residents performing employment activities in Belgium.

45. In that sense, the individuals will receive a tax reduction in the Netherlands if the tax burden on this income is higher in Belgium than what it would be if the activity were developed in the Netherlands.[30]

46. This compensation scheme is interesting because by doing so the Dutch government recognises that Dutch residents performing employment activities abroad should be taxed in the same manner as employees performing activities within the country.

47. By doing so, The Netherlands fulfils the goal of fairly dividing the tax burden between the countries, while guaranteeing that the shared tax competence of a country will not be prejudicial to its residents. This is an interesting practice that could be copied by other countries.

IV France

48. In the current report, France presented an additional challenge, as apart from the information provided by the Belgian authorities concerning the number of Belgian Frontier Workers performing employment activities on the French side of the border, there exists no up to date information on the number of frontier workers from the border countries under the scope of this -up-to-date- report who work in France (this information was neither found on French statistical websites nor on the German, Luxembourgish and Swiss sites). Information regarding French frontier workers performing employment activities, on the other hand, is readily available.

49. Despite this lack of date on the inbound frontier workers in France, it is still possible to analyse how the French government has negotiated with treaty partners the allocation of taxation rights over the employment income of frontier workers. On that matter, in this section, I will refer to the tax treaties signed with Germany, Luxembourg and Switzerland. For information regarding the France-Belgium treaty please refer to section III.1.

1. Frontier workers on the French-German border

50. As mentioned above, it was not possible to find the information on the number of French resident frontier workers performing employment activities in Germany, but it is known that in 2013 there were

29 Rijksinstituut voor ziekte en invaliditeitsverzekering, available at
<https://www.riziv.fgov.be/SiteCollectionDocuments/statistieken_grensarbeiders_2017.pdf>
30 Article 27, Double Tax Convention Belgium-Netherlands.

37,800 German resident frontier workers performing their employment activities in France[31], and in 2017 this number increased to 46,000.[32]

51. Regarding the taxation of employment income, the general rule is that taxation shall occur exclusively in the country of employment[33], unless the employee resident in a contracting state is present in the country of employment for less than 183 days, the remuneration is paid by or on behalf of an employer not resident in the country of employment and not borne by a permanent establishment or a fixed base which the employer has in the country of employment.[34]

52. There are also special rules for frontier workers, who should be taxed exclusively at their country of residence if they work abroad and have their permanent home in the country of residence[35]. As for the definition of frontier zone, this covers municipalities which are wholly or partly no more than 20 kilometres from the frontier[36], with this threshold being extended to 30 kilometres in the case of individuals with permanent homes in France performing employment activities in Germany[37].

53. Unlike the tax treaties that we have already examined, the agreement between France and Germany introduces an innovation with regard to the allocation of taxation rights between the countries. The convention prescribes that the country of residence of the frontier worker shall pay to the country of employment an annual compensation of 1.5% of the gross annual remuneration of the frontier worker[38], and that this gross annual remuneration will be determined by means of the information provided by the employers to the respective tax authorities.[39]

54. Furthermore, the countries agree to settle by mutual agreement the measures necessary to implement these rules and to meet at least once every five years to ensure that 1.5% of the annual gross remuneration of the employee does not result in a compensation higher than 44% of the tax levied on the total amount of the gross annual remuneration of frontier workers referred afore. If that happens, the compensation shall be reduced.[40]

55. The system implemented by this treaty is an interesting one, as it guarantees that both countries will benefit from the tax levied on the income earned by frontier workers, while avoiding the complexities of dealing with the crediting of taxes paid abroad. In that sense, this system seems better suited to allocating taxation rights fairly between the countries concerned, while guaranteeing that the individuals will not suffer any double taxation on their employment income.

56. Additionally, the cap put on the compensation guarantees that most of the tax revenues will remain with the country of residence of the frontier worker, which most likely will incur more expenses for the benefit of the frontier worker than his/her country of employment.

57. There is still no system of compensation or retrocession provided. However, it should be noted that a financial compensation by the French administration concerning almost 70,000 former French border workers has been established. These persons will now be taxed only at their place of residence. Conversely, taxpayers receiving a French pension in Germany will not be taxed in Germany.

2. Frontier workers on the French-Luxembourgish border

58. French-resident frontier workers constitute the majority of the frontier workers employed in Luxembourg, amounting to 94,901 individuals (according to the Luxembourg Public Statistics.[41])

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31 Mission Opérationelle Transfrontalière, available at <http://www.espaces-transfrontaliers.org/uploads/tx_tmswmotressources/map/carte_flux_france_2018.pdf>
32 Les Echos, Le Travail Frontalier Français Profite aux Habitants du Nord-Est, available at < https://www.lesechos.fr/20/12/2017/lesechos.fr/0301037677930_le-travail-frontalier-francais-profite-aux-habitants-du-nord-est.htm >.
33 Article 13(1), Double Tax Convention France-Germany
34 Article 13(4), Double Tax Convention France-Germany
35 Article 13(5)(a), Double Tax Convention France-Germany.
36 Article 13(5)(b), Double Tax Convention France-Germany.
37 Article 13(5)(c), Double Tax Convention France-Germany.
38 Article 13A(1), Double Tax Convention France-Germany.
39 Articles 13A(3) and 13A(4), Double Tax Convention France-Germany.
40 Article 13A(6), Double Tax Convention France-Germany.
41 Luxembourg Public Statistics, available at < https://statistiques.public.lu/catalogue-publications/regards/2018/PDF-13-2018.pdf>

59. Despite this substantial importance of French frontier workers to the Luxembourgish economy, there are no special rules for the taxation of frontier workers; they are under the general rule of the double tax convention signed between the parties.

60. According to Article 15 of this agreement, employment income shall be taxed exclusively where it is carried out,[42] and a personal occupation is only carried out in a country if it has a fixed base available in that country.[43] Surprisingly, as it is a requisite for taxation at the source country, the treaty contains no definition of what such a fixed base is. If it is considered that the employment is not carried out in the country of employment, the country of residence of the worker will have exclusive taxation rights over his income.[44]

61. Once again France resorted in its tax treaties to the attribution of exclusive taxation rights to one of the treaty partners, a formula which, as mentioned afore, although practical does not consider that a frontier worker will generate expenses to both countries.

62. There is still no system of financial compensation. This topic is currently part of an ongoing debate, in the context of which, in 2019, the mayors of Metz and Trier have sent an open letter to Emmanuel Macron and Angela Merkel.

3. Frontier workers on the French-Swiss border

63. Like the situation in Luxembourg, French resident frontier workers account for most of the frontier workers currently employed in Switzerland, totalling 172,523 persons.[45]

64. The treaty between France and Switzerland is applicable to taxes on income imposed by the confederation, the cantons and municipalities, which serves to reassure individuals that the countries will act to avoid double taxation that may be caused by the imposition of taxes in any of those levels.

65. The general rule for taxation income from employment is based on the OECD model mentioned above ; exclusive taxation at the country of residence unless the activities are exercised at the country of employment.[46] And even if that is the case, the country of residence may still have exclusive taxation rights if the employee is present in the country of employment for less than 183 days, the remuneration is pay by, or on behalf, of an employer not resident in the country of employment and it is also not borne by a permanent establishment or fixed base of the employer at the country of employment.[47]

66. The treaty also contains a special rule to frontier workers, which are subject to the agreement concerning the taxation of remuneration of frontier workers, signed in 1983. According to this agreement, which bound the Swiss Federation, who was acting on behalf of the cantons of Berne, Soleure, Basel, Vaud, Valais, Neuchatel and Jura; income from salaries, wages and other similar remuneration received by frontier workers shall be taxable only in the employee's country of residence, which in turn will pay a compensation to the country of employment of 4.5% of the total gross annual remuneration earned by frontier workers. Furthermore, the agreement clarified the meaning of the term frontier worker, which is "any person resident in a country who carries on a salaried activity in the other State for an employer established in that other country and who, as a general rule, returns daily to the State in which (s)he is resident".

67. In 2007, the French government published a guideline stipulating that the exemption from tax at the source country was conditional on the presentation of a certificate of residence provided by the tax authority of the country of residence.

68. The canton of Geneva was not part of this agreement, as it has previously signed a separate agreement with the French government through which it pays a compensation to the French Government amounting to 3.5% of the gross annual remuneration earned by frontier workers.[48] Differently from the agreement signed by the Swiss Federation, Geneva is the only party obliged to

42 Article 15(1), Double Tax Convention France-Luxembourg.
43 Article 15(2), Double Tax Convention France-Luxembourg.
44 Article 18, Double Tax Convention France-Luxembourg.
45Bundesamt für Statistik, Grenzgängerinnen und Grenzgänger, available at < https://www.bfs.admin.ch/bfs/de/home/statistiken/arbeit-erwerb/erwerbstaetigkeit-arbeitszeit/erwerbstaetige/schweizer-innen-auslaender-innen/grenzgaenger-innen.html>.
46 Article 17(1), Double Tax Convention France-Switzerland.
47 Article 17(2), Double Tax Convention France-Switzerland.
48 Article 1(C), Agreement between the Swiss Federation and the French Republic on the financial compensation regarding frontier workers in Geneva, available at <http://crfginfo.org/prod/sites/default/files/documents/accord_compensationfinanciere_1973.pdf>

transfer 3.5% of the gross annual remuneration earned by frontier workers therein; France does not have the same obligation.

69. Ultimately, the scheme adopted for the taxation of the employment income from frontier workers is like the one previously adopted in the French-German Double Tax Convention. Likewise, this system is practical while guaranteeing that both countries will benefit from the taxation of the employment income earned by frontier workers.

V Germany

70. Germany is the country in our report with the most border regions with a great influx of individuals from the other countries examined in the report. Since the double tax conventions between Germany-France and Germany-Belgium have already been analysed, in this chapter reference will be made solely to the treatment of frontier workers in relations involving Luxembourg, The Netherlands and Switzerland.

1. Frontiers workers on the German-Luxembourgish border

71. The flux of frontier workers between Germany and Luxembourg is characterised by a considerable number of German residents working in Luxembourg (43,800, [49]) with much less movement in the opposite direction (216). [50]

72. Furthermore, there are no special rules concerning frontier workers, who are subject to the general rule of the double tax convention article on employment income. According to this article, employment income is taxed exclusively at the country of residence of the employee unless the activities are exercised at the country of employment[51]. And even if that is the case, the country of residence may still have exclusive taxation rights if the employee is present in the country of employment for less than 183 days, the remuneration is pay by, or on behalf, of an employer not resident in the country of employment and it is also not borne by a permanent establishment or fixed base of the employer at the country of employment.[52]

73. As mentioned afore, this system may sacrifice a shared competence on behalf of practicality, but if the conditions of Article 14(2) are not fulfilled it will strike a balance between the taxation powers of the countries.

74. There is still no system of financial compensation in this case.

2. Frontier workers on the German-Dutch border

75. Once again there are many more German frontier workers abroad than residents of the other country working in Germany, achieving in this case a 3:1 proportion (34,000 German residents working in the Netherlands and 11,000 Dutch Residents working in Germany.[53])

76. The general rule for taxation of employment income is the same one adopted in the treaty explained in the previous section, namely that employment income is taxed exclusively at the country of residence of the employee unless the activities are exercised at the country of employment.[54] And even if that is the case, the country of residence may still have exclusive taxation rights if the employee is present in the country of employment for less than 183 days, the remuneration is pay by, or on behalf, of an employer not resident in the country of employment and it is also not borne by a permanent establishment or fixed base of the employer at the country of employment.[55]

49 Luxembourg Public Statistics, available at < https://statistiques.public.lu/catalogue-publications/regards/2018/PDF-13-2018.pdf>.
50 Interregionale Arbeitsmarktebeobachtungsstelle, “Die Arbeitsmarktsituation in der Grossregion, Grenzgängermobilität”, available at
< https://www.iba-oie.eu/fileadmin/user_upload/Berichte/10._IBA-Bericht__2016__/IBA_Grenzgaenger_DE_web.pdf >.
51 Article 14(1), Double Tax Convention Germany-Luxembourg.
52 Article 14(2), Double Tax Convention Germany-Luxembourg.
53 Centraal Bureau voor de Statistiek, “Factsheet Grensoverschrijdende Arbeid”, available at < https://www.cbs.nl/nl-nl/achtergrond/2017/07/factsheet-grensoverschrijdende-arbeid>.
54 Article 14(1), Double Tax Convention Germany-Luxembourg.
55 Article 14(2), Double Tax Convention Germany-Luxembourg.

77. Nonetheless, unlike the German tax treaty with Luxembourg, this treaty prescribes, as a rule, the exclusive taxation of employment income at the country of residence of the income earner, considering that the payment is borne by a permanent establishment situated in a cross-border economic area through which the common border of the two countries runs. If, however, the European regulations on social security determine that the individual is subject to the legal provisions of the country of employment, this country may also tax the employment income of the individual.[56]

78. Furthermore, if the total tax burden in Germany exceeds the amount which The Netherlands would tax, if the income had been earned in the latter, the individual may opt for a tax relief to be granted by The Netherlands.[57]

79. Hence, the current rules guarantee that the taxpayer will not face a higher tax burden due to his cross-border activities as well as make recourse to rules on social security to determine whether the taxation rights will be granted exclusively to one country or will be shared between them.

3. Frontier workers on the German-Swiss border

80. There was no information available regarding the number of Swiss resident frontier workers who perform their employment activities in Germany, but in the past year there were 60,203 German resident frontier workers in Switzerland.[58]

81. The general rule adopted for the taxation of employment income is the one prescribed by the OECD Model Tax Convention, i.e. exclusive residence taxation, unless the employee is present in the source country for a period longer than 183 days or payments are made by, or on behalf, of a resident of the country of employment or borne by a permanent establishment or fixed base of the employer in the country of employment.[59]

82. Apart from these, there are special rules for the taxation of the employment income of frontier workers. On that matter, it is prescribed that the country of residence of the employee and the country of employment may both tax the employment income, but the latter will only be allowed to levy a tax up to 4.5% on the gross amount of the remuneration earned by the individual in case the country of residence confirms that the individual is indeed residing therein.[60]

83. Two compensation systems exist. For German cross-border workers in Switzerland, the deduction made in Switzerland is deducted from German withholding tax. On the other hand, the few Swiss residents who work as frontier workers in Germany are taxed in Switzerland for only 80% of their gross remuneration, again to offset the 4.5% levied on them in Germany.

84. The treaty also provides a definition of the term frontier worker, which is any person resident in a Contracting State who has a place of employment in the other Contracting State and regularly returns to his residence. Also, if the person does not return to his/her residence following the end of the working time, the status of frontier worker shall cease to apply only if that person, in the case of employment for a full calendar year, does not return to his/her residence on more than 60 working days because of the employment.[61]

85. The system created by the Germany-Switzerland tax treaty is a hybrid one, as it prescribes a shared tax competence while limiting the maximum rate of tax which the country of employment may apply. In that sense, the system intends to guarantee that both countries will receive tax proceeds from the frontier workers, but that most of the taxation rights shall be with his/her country of residence. The system seems to achieve this goal, although questions may arise concerning its complexity.

VI Liechtenstein

86. Liechtenstein only has a border with one of the other countries analysed in the report, Switzerland. And differently from the cases studied up until now, the flux of frontier workers between the countries

56 Article 14(3), Double Tax Convention Germany-Netherlands.
57 Article XII, Protocol to the Double Tax Convention Germany-Netherlands.
58 Bundesamt für Statistik, Grenzgängerinnen und Grenzgänger, available at < https://www.bfs.admin.ch/bfs/de/home/statistiken/arbeit-erwerb/erwerbstaetigkeit-arbeitszeit/erwerbstaetige/schweizer-innen-auslaender-innen/grenzgaenger-innen.html >.
59 Article 15, Double Tax Convention Germany-Switzerland.
60 Article 15a(1), Double Tax Convention Germany-Switzerland.
61 Article 15a(2), Double Tax Convention Germany-Switzerland.

is balanced, with around 8,308[62] Liechtenstein resident frontier workers exercising their employment in Switzerland and around 10,000 Swiss resident frontier workers exercising their employment activities in Liechtenstein.[63]

87. The general rule adopted for the taxation of employment income is the one prescribed by the OECD Model Tax Convention, i.e. exclusive residence taxation, unless the employee is present in the source country for a period longer than 183 days or payments are made by, or on behalf of, a resident of the country of employment or borne by a permanent establishment or fixed base of the employer in the country of employment.[64]

88. As for the taxation of frontier workers, the convention prescribes that the income of the individuals that have their home in a contracting country and work in another and travel to the latter, as a rule, every working day, shall be levied exclusively at their country of residence.[65] Furthermore, the Protocol to the treaty stipulates that: "a person ceases to be a frontier worker if, for work-related reasons, (s)he does not return to his/her home at the end of his/her work on more than 45 working days per calendar year".

VII Luxembourg

89. The relations between Luxembourg and its neighbouring countries is evaluated above in sections III.3 (Luxembourg-Belgium), IV.2 (Luxembourg-France) and V.1 (Luxembourg Germany).

VIII Netherlands

90. Since the current report has analysed the allocation of taxation rights regarding employment income of Dutch resident frontier workers, in sections III.4 (Netherlands-Belgium) and V.2 (Netherlands-Germany) above, it is not necessary to repeat what has already been said. For a better understanding of the tax issues concerned, please refer to these sections.

IX Switzerland

91. For more information on the allocation of taxation rights over employment income of frontier workers in Switzerland, see sections IV.3 (Switzerland-France), V.3 (Switzerland-Germany). and VI (Switzerland-Liechtenstein) above.

X Taxation of income from frontier workers: avoiding of double taxation and allocation of taxation rights

92. In the previous sections, we have focused on the agreements made between Belgium, France, Germany, Liechtenstein, Luxembourg, The Netherlands and Switzerland concerning the taxation of frontier workers in their respective borders. In this section, we will reflect on the choices made by countries as regards the allocation of taxation rights between them, how these comply with the goal of avoiding double taxation of individuals who decide to perform activities abroad and eventual issues that may arise, from the perspective of the countries, based on these agreements. At this point it is important to highlight that the current analysis will focus on the perspectives of the taxpayers and the authorities concerned.

93. With regard to the avoidance of double taxation of the individual, when dividing amongst themselves the right to tax the income earned by frontier workers, countries made use of three main systems: (i) exclusive taxation, in the country of residence of the frontier worker or in the country of employment (source country of income); (ii) shared taxation rights, including a situation in which the country of residence of the frontier worker will provide him/her with a tax relief as a means to guarantee that (s)he will not be worse off by working as a frontier worker (the Dutch approach in double tax

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62 Bundesamt für Statistik, Grenzgängerinnen und Grenzgänger, available at < https://www.bfs.admin.ch/bfs/de/home/statistiken/arbeit-erwerb/erwerbstaetigkeit-arbeitszeit/erwerbstaetige/schweizer-innen-auslaender-innen/grenzgaenger-innen.html >.

63 KPMG Switzerland, Liechtenstein & Schweiz: Grenzgänger oder Nichtgrenzgänger?, available at < https://blog.kpmg.ch/tax-legal-news/liechtenstein-schweiz-grenzganger-nichtgrenzganger/>.

64 Articles 15(1) and 15(2), the Double Tax Convention Liechtenstein-Switzerland.

65 Article 15(4), Double Tax Convention Liechtenstein-Switzerland.

conventions with Belgium and Germany); and (iii) exclusive taxation with a compensation scheme between the countries.

94. The system of exclusive taxation prescribes that either the income is taxed solely at the country of residence of the employee (for example France-Belgium treaty) or in the country of employment (for example France-Luxembourg treaty). Taxation in only one of the countries certainly fulfils the objective of avoiding double taxation of the income earned by the individual, but it fails to recognise that the individuals presence in both countries already leads to expenses being incurred by the countries in favour of this individual, and that due to the attribution of exclusive taxation rights one of the countries is prohibited from charging the individual due to these costs. It also has as a bonus the fact that exclusive taxation in one of the member States helps to simplify the tax system, as taxpayers wont need to compile documents to prove their right to a credit for taxes paid abroad and the tax authorities wont need to verify the existence and validity of the credits. On the other hand, the restriction on the taxation rights of the country of employment hampers the sovereignty of this country to levy taxes over the economic activities developed in its territory.

95. Furthermore, the choice between exercising exclusive taxation rights at source or residence brings certain issues to the forefront of tax discussions. In that sense, taxation at residence should guarantee that all individuals who are resident in the same place will be taxed in the same manner, which leads to an equal treatment of these persons. Also, taxation at residence is in line with the ability of individuals to pay, and with a progressive tax system, as the ones that can pay more taxes will do so, considering the total amount of income earned worldwide. Such taxation also guarantees that resident persons, who benefit the most from the expenses made by the government, will fund these expenses through taxes. On the other hand, residence taxation significantly complicates tax compliance, and the country of residence is highly dependent on the transfer of information from the source country to know how much it should tax, but the latter has no incentive to provide this information as it will not have taxation rights over this income.

96. As for the granting of exclusive taxation rights to the source country, it guarantees that taxation will occur in the place in which the income is effectively earned, aligning taxation rights to income creation. Furthermore, it guarantees that persons who earn income in one specific jurisdiction, hence compete in this jurisdiction, will be subject to the same tax burden, eliminating potential distortions caused by taxes eventually applied by the country of residence of the income earner. This form of taxation is also administratively simpler, generating less compliance costs to the taxpayer and enabling the tax authorities to swiftly verify whether taxes are effectively being paid, without dependence on provision of information by another country. As a downside, source taxes will most likely not reflect a taxpayer´s ability to pay, as the source country will only be aware of income earned by the taxpayer in its territory. Additionally, this form of taxation will sever the link between benefits earned by the taxpayer and the financing of these benefits, as it can be assumed that the country of residence provides more benefits for taxpayers than the source country.

97. Regarding the sharing of taxation rights between countries, there are also two possibilities: the traditional one, in which neither country is restrained in its right to tax because the conditions for exclusive taxation at residence were not fulfilled (for example the German-Luxembourg treaty and the Liechtenstein-Switzerland treaty) and an innovative one in which, in spite of the shared taxation rights, the country of employment is limited as to the amount of tax that it can levy (for example the Germany-Switzerland treaty).

98. In both situations, the avoidance of double taxation is conditioned to the acceptance, by the country of residence, that taxes paid have the same value as taxes paid domestically, i.e. taxes paid abroad can reduce the domestic tax liability of individuals, which intrinsically results in an increase of the complexity of the tax system for taxpayers and tax authorities and entails the risk that the country of residence would not provide a credit for the full tax paid in the country of employment, generating double taxation over this income and putting the individual performing employment activities abroad in a less advantageous situation when compared with the resident in a country and performing activities therein.

99. The scheme adopted by the Netherlands, in which Dutch residents get a tax reduction in the Netherlands if the tax burden on income earned abroad is higher than what it would have been in a domestic situation (for example Belgium-Netherlands and Germany-Netherlands tax treaties), is a step in the right direction from the perspective of the taxpayer, but it presents an issue for the tax authorities of the country of residence as they will ultimately reimburse, from their own budget, a tax paid in another country and that they will never collect.

100. It is worth noting that this problem would not be solved by the establishment of a clearing mechanism or compensation scheme between the residence and country of employment, since, if such a system were in place, it would amount to a restriction on the taxation rights of the country of employment, based on the non-taxation of the income by the country of residence, which would constitute an infringement of the tax sovereignty of the country of employment to tax the activities that are carried out in its territory.

101. Finally, in some of the treaties it was prescribed that only one country would be entitled to tax the income of the frontier workers, but this country had the obligation to forward part of the tax collected to the other country. The collecting country could be the country of employment (France-Geneva agreement) or the country of residence of the employee (France-Germany and France-Switzerland treaties). This compensation mechanism brings an interesting perspective on the matter, as it fulfils at the same time the idea of avoiding the double taxation of the income, which favours the taxpayer, in a more streamlined manner, reducing the compliance obligations of taxpayer and the supervision costs of tax authorities, which would not need to verify the situation of each individual to assess how much tax it should collect/provide a credit for.

102. Taking the aforementioned into consideration, it seems that this system implemented between France, Switzerland and Germany in their bilateral relations is the one that better fulfils the goals of avoiding double taxation while guaranteeing, in a less complex manner, that countries will also be entitled to achieve revenue to pay for the expenses incurred in favour of the taxpayers. Nonetheless, it is important to bear in mind that there is no one-size fits all approach on the matter, and the option between the systems will depend on the economic relations between the parties involved. A good example of this are the different tax rates prescribed by the Germany-Switzerland treaty and the France-Switzerland treaty.

103. In line with this thought, it is also inadequate to determine which method would lead to a “fair” allocation of taxation rights, as the “fairness” would be dependent on the balance/imbalance of the economic relation of the parties and the modalities of access to social security benefits, so the decision on this division of taxation rights must be made on a case-by-case basis.

CONCLUSION

104. In the previous sections, it has been made clear that the balance between the avoidance of double taxation and the allocation of taxation rights between the jurisdictions involved is challenging. The great dilemma faced by taxpayers and tax authorities is to find a way in which double taxation is avoided, while the countries of residence and employment will still be able to exercise taxation rights over income earned by non-residents/residents.

105. The study of the treatment of income from employment on the double tax conventions signed between countries with highly mobile frontier workers demonstrates that while, in general, the treaties and agreements signed are successful in guaranteeing that taxpayers are not worse off by living in one country and working in the other, i.e. double taxation is avoided, this is normally achieved by overlooking the perspective of the tax jurisdictions, which have their taxation rights restricted.

106. An analysis of double tax conventions shows that, at present, countries normally exclude the taxation rights of one of them by means of an exemption (at residence or source) or allowing for concurrent taxation of this income, with a subsequent provision of a credit for the taxes paid at source. Although the former solves the double taxation issue, it restricts the taxation rights of jurisdictions that are indeed having expenses related to the frontier workers. On the other hand, the latter, while allowing both countries to tax, might lead to double taxation and an overcomplication of the tax system.

107. But there is also a third possibility, which is not often used, namely to exclude the taxation rights of a country and to promote a redistribution of income amongst them. This solution avoids, in general, the double taxation issue, while simplifying the compliance aspect, since all information necessary for the division of the income is already in the hands of the tax authorities. Despite these benefits, it is important to bear in mind that this solution might not be applied to all bilateral relations between the countries, as the differences in their tax policies and the level of their economic integration might not allow for the adoption of such a system.

108. It remains clear that, to satisfy both the desire of taxpayers and tax authorities, the avoidance of double taxation and allocation of tax rights will need to be done in a coordinated manner. This will allow all jurisdictions involved to receive tax income from activities arising in their territories and ensure that

the country of residence of individuals, the country that initially provided the possibility for them to develop and subsequently work abroad, is also not excluded from taxation.

109. The big issue then becomes what amount should be taxed by each country. This will vary depending on the economic relations between the countries, so there is no single answer to the question. If there is a reciprocal flow of frontier workers between them, it is natural that countries would find common ground more easily. While in the case of frontier workers flowing predominantly in one direction, which is the case in most of the situations studied here, countries may find it difficult to define how much should be taxed in each place.

110. Taking this into consideration, it may be advisable to deal with the issue of frontier workers in a more collaborative and coordinated setting; be it at a local or in a broader European level. The core of this issue is that, to achieve a balanced allocation of taxation rights while avoiding double taxation, countries should not act unilaterally or in strict bilateral settings. All participants stand to gain by acting in a coordinated way.

111. A particularly interesting approach, in terms of intensifying co-operation, is the creation of integrated cross-border areas, with their own resources for the development of real cross-border territory projects, particularly with regard to mobility and spatial planning, as implemented in Geneva, which are known as Local Groupings of Cross-border Co-operation (GLCTs).

112. The competence and scope of the Greater Geneva GLCT are recognised in the three cross-border areas of mobility, spatial planning and the environment. More generally, this new governance body reinforces existing bodies and enables local authorities in Switzerland and France to ensure cross-border co-development over time and thus better meet the needs of their residential areas.

113. However, the question of the need for this new cross-border co-operation body to have its own tax system has now arisen. A certain number of Swiss and French territorial actors seem favourable and consider that this development would allow them to cross a major milestone in the Greater Geneva cross-border conurbation project.

114. In this perspective, the Greater Geneva GLCT could eventually represent a unique case in Europe of a cross-border metropolis, straddling two states, with its own financial autonomy and decision-making powers, to govern its development and decide its own investments structuring. [66]

66 Convention establishing the "Franco-Valdo-Genevan conurbation project" Local Cross-border Co-operation Grouping (GLCT) with a view to ensuring its governance, 23 November 2011. As regards the institutional functioning, the GLCT Bureau consists of the President (elected from representatives of the Canton of Geneva) and seven vice-presidents, representing each constituent partner of the GLCT. The 26 elected Swiss and French members of the bureau sit on the GLCT Assembly equally. The partners of the Greater Geneva GLCT, besides the Swiss Confederation and the French State, which sit as associate members, are respectively: the Republic and Canton of Geneva, the City of Geneva, the Canton of Vaud, the Regional Council of the District of Nyon, the Metropolitan Pole of the French Genevois, the Auvergne-Rhône-Alpes Region, the County Council of Ain and the County Council of Haute Savoie.