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BRAIN DRAIN TAX VS. BRAIN GAIN BENEFITS: GENERAL THOUGHTS FROM A SPANISH PERSPECTIVE

One might expect that tax benefits introduced by certain developed countries to attract foreign high-skilled workers would run contrary to taxes aimed at the alleviation or deterrence of so-called brain drain. This article shows, however, that this is not necessarily the case: brain gain benefits might be justified by the existence of home-state brain drain taxes and, at the same time, serve to alleviate international double taxation generated by this type of taxes.

Key words: *Brain drain tax. – Brain gain tax benefits. – High-skilled workers taxation. – Highly mobile individuals taxation. – Inpatriates.*

1. INTRODUCTION

The core of the proposal envisaged by Prof. Bhagwati more than 40 years ago is well known: “(...) the loss to the less developed countries of some of their best-trained citizens can be made up by a tax on emigrants, with the revenues channeled back home through the United Nations.”[1] Since then there has been no shortage of publications complimenting, criticizing and (more frequently) building new models based upon that original idea.[2] However, the discussion on the very phenomenon of brain

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[1] Bhagwati (1976, 34–38).

[2] A good revision in Brauner (2010, 221–268).

drain taxation and the corresponding technical alternatives to articulate it have largely remained academic, inasmuch as no single jurisdiction has seriously implemented legislative measures in this direction. Quite the contrary: the policy of many developed states, and indeed a large part of EU countries, has been to design an entire arsenal of tax incentives to attract talent (*brain gain benefits*). Namely, these countries may accord a beneficial tax treatment for "new residents" postponing the full effect of ordinary residence, thereby limiting personal income taxation on domestic sources of income or even taxing these immigrants at reduced tax rates, all of this aimed at promoting the arrival of high-level professionals (sometimes including even sportspersons).[3]

We would therefore be facing two tax policies – "brain drain taxes" and "brain drain benefits" – which at first glance are radically opposed. However, and this is the suggestion of this contribution, the legal configuration of the Spanish brain gain benefits might well help to overcome some of the technical difficulties frequently perceived in certain versions of brain drain taxes.

The rest of this article is organized as follows: section 2 briefly exposes the main features of the Spanish tax treatment of highly mobile individuals placing the emphasis on the description of brain gain benefits. Section 3 analyzes the eventual coexistence of these benefits with different versions of brain gain taxes, with a view to detecting a clash or rather a synergy of (tax) policies. Section 4 contains a brief conclusion.

2. SPANISH TAX TREATMENT OF HIGHLY MOBILE INDIVIDUALS AND BRAIN GAIN BENEFITS

In a globalized world, immigration of skilled workers is far from being the matter of migration from developing to developed countries. It is much more a matter of attraction of high-qualified workers wherever they are and of retention of these types of workers, preventing their emigration.

In order to achieve these goals, states implement different kinds of measures. Among these measures, tax policy is one of the most relevant and Spain has set up a number of special tax regimes to deal with this phenomenon: tax rules (incentives and disincentives) to retain talent, on the one hand; and tax rules (incentives) to attract talent.

Regarding the tax measures to retain talent and more specifically, the tax disincentives, Spain has basically set up three exit taxes, which have been very problematic from a EU tax law perspective:[4] 1) expanded

[3] Falcón y Tella (2009).

[4] On these and other Spanish exit taxes see CJEU, case C-269/09, European Commission v. Kingdom of Spain.

residence for taxpayers who move their residence to a tax haven;[5] 2) a special timing rule, taxing unrealized income in case of loss of residence;[6] 3) a specific rule taxing unrealized capital gains on shares with a market value of at least 4,000,000 €.[7]

The previously mentioned tax measures deal with international mobility of workers but they are by no means focused on the phenomenon of brain drain. These measures accent on mere "collection drain".

Regarding the tax measures to retain talent by granting tax incentives, Spain has set up a special regime for expatriates.[8] However, the previous tax incentive focuses more on supporting Spanish companies in their process of internationalization than on providing tax incentives to retain talent.

The only tax measure actually related to incentivizing international mobility of (skilled) individuals is the one first introduced in 2004, in Article 93 of the PITA, whose relevance for this contribution recommends a closer examination. Any individual residing in Spain for personal income tax purposes would in principle be taxed on their worldwide income, at a maximum rate of around 45%, depending on the particular region in which the individual is a resident[9]. In very broad terms the special regime consists on an option for inpatriates fulfilling certain requirements to be taxes as non-residents: therefore these individuals may choose between being taxed as ordinary residents, at a progressive rate of up to 45%, on worldwide income, or, if deemed non-residents, at a proportional rate of 24% on Spanish income sources.[10] The regime has been heavily criticized since its inception and this explains to a large extent its successive amendments, the most noteworthy being: 1) the introduction of a maximum threshold of 600,000 euros in 2010 regarding the special tax rate; the limit, certainly explained by the critical situation of Spain since 2009, implied the existence of a dual track tax rate: i.e.

[5] Art. 8.2 of the Law 35/2006, of 28 November 2006, del Impuesto sobre la Renta de las Personas Físicas y de modificación parcial de las leyes de los Impuestos sobre Sociedades, sobre la Renta de no Residentes y sobre el Patrimonio (Personal Income Tax Act, hereinafter PITA).

[6] Art. 14.3 of the PITA. This rule is not without EU Law compatibility issues and it has been in fact revised in view of several decisions of the Court of Justice of the European Union considering similar rules of other Member States in breach of the EU freedom of establishment.

[7] Art. 95 *bis* of the PITA.

[8] Art. 7 p) of the PITA. For an analysis of this tax incentive, see López López (2015, 94–140).

[9] The different rates for PITA purposes are derived from the particular Spanish partially decentralized personal income tax system.

[10] This special regime also applies to the Spanish Impuesto sobre el Patrimonio (Capital Tax) whose high minimum exempt amount and low rates makes it practically irrelevant.

24% on source income up to 600,000 euros, and 45% above that figure. 2) in 2015 sportspersons were excluded to this tax regime; this change was the result of an obvious misalignment between the theoretical goal of the benefit – attracting highly-skilled professionals – and its effect in practice – the almost exclusive application to sportspersons, particularly football players.[11]

Beyond the fact that the special tax regime will in practice preclude the application of the Spanish double tax convention network to residents opting for it,[12] the rule has been harshly criticized from a strict constitutional perspective. Since its seminal Decision of 26 April 1990 (STC 76/1990) the Spanish Constitutional Court has repeatedly made clear that: a) the equality principle imposes the application of the same legal (tax) consequences to comparable factual situations; b) the principle of equality does not prohibit any differential legal treatment but only discriminations that may be considered artificial or unjustified for not being based on objective and reasonable criteria; c) for a different treatment to be in compliance with the constitutional principle of equality, it is not enough that it is objectively and reasonably justified, since the legal consequences of such treatment must be suitable and proportional to the pursued goal.

In a nutshell, according to the Spanish Constitutional Court, just the different (tax) treatment of comparable situations might be considered a violation of the Constitution if that different treatment is either not justified or justified but not proportional. Even if the Spanish Constitutional Court has not yet had the opportunity to rule on the special inpatriate regime, the application of the aforementioned case law should lead to a straightforward conclusion according to the following reasoning. Comparing the situation of an ordinary tax resident earning an income that is comparable (although not identical) to that of a resident inpatriate opting for the application of the special regime, it is obvious that the two taxpayers are treated differently. The former will be taxed on their worldwide income at a progressive tax rate of up to 45%. The latter will be taxed a 24% tax rate on Spanish-source income on the first 600,000 euros. The Spanish-source income exceeding 600,000 will be taxed at a

[11] It is with good reason that the special tax regime received, at least before 2010, was called the Beckham Law, being this British football player was one of the first and most prominent beneficiaries of the regime.

[12] In fact, Article 120 of the Reglamento del Impuesto sobre la Renta de las Personas Físicas (PIT regulations hereinafter) allows for the issuing of a certificate of residence for beneficiaries of the special regime. This certificate, however, is not proof the residence in Spain for double taxation conventions purposes, according to the very regulations. Some scholars and practitioners in Spain have been extremely critical of this restriction, not only in regard to Spanish double taxation conventionss lacking Article 4(1)2 of the OECD Model Tax Convention. See Falcón y Tella (2010, 49–50).

rate of 45%. Even if the preamble to the law introducing the special inpatriate regime in Spain did not mention its purpose, there is a broad consensus among both tax authorities and scholars that the measure intends to attract high-skilled workers to Spain.[13] However, it is more than doubtful whether the special tax regime is actually adequate for such attraction, taking into account that the very scope of the measure does not differentiate the workers who might benefit from the special tax regime. The amendment introduced in 2015 – exclusion of sportspersons – merely corrected the initial roughest mistakes of the regime, which, however, remains incapable of objectively defining the criteria referring the high-skilled workers that it theoretically aims to benefit. Finally, and most importantly, the differences in taxation between regular residents and inpatriates opting in for the special regime – which has additionally dragged on for six years – seem too great for them to be considered proportional. The amendment made in 2010 – dual rates for income below and above 600,000 € – does not seem to sufficiently alleviate this lack of proportion, particularly if taking into account that among the 2,000 persons who had enjoyed the regime before 2010, less than 10 percent had incomes above 600,000 €.[14] This would suggest that especially after 2015, with the exclusion of sportspersons, the regime in practice essentially consists of the application of the reduced rate (24%) on Spanish-source income.

At this point it can only be concluded that Spain lacks a clear policy regarding taxation of cross-border mobile individuals and that the only measure that seems at least to show a more or less clear intention is of questionable constitutionality.

3. BRAIN DRAIN TAXES AND BRAIN GAIN BENEFITS TO THE (MUTUAL) RESCUE

One might expect that brain gain benefits, such as those described for the Spanish tax system, are by definition the opposite of brain drain taxes. Ultimately, both sets of tax measures would serve different and rather contradictive policies, namely to deter the brain drain, for the benefit of developing countries,[15] and to promote it at their expense. However, as we will try to prove, this would only hold true regarding a particular and rather outdated version of brain drain taxes, whereas, in

[13] See, among others, Álbarez Barbeito, Calderón Carrero (2010, 17–18), Sanz Clavijo (2013); Gorospe Oviedo (2010, 15–48); García Carretero (2015, 93).

[14] Falcón y Tella (2009).

[15] Explicitly recognized as one of the goals of the original Bhagwati tax proposal: Bhagwati, Dellalfar (1973, 95).

their evolved versions, brain gain benefits and brain drain taxes could be rather complementary.

3.1. The Original Bhagwati Proposal and Brain Gain Benefits

In brief, the original Bhagwati brain drain tax proposal implied the imposition of a tax on the income of immigrants, collected by the tax authorities of the developed host state and transferred to the developing home state.[16] It is highly evident that a host-state brain drain tax such as the original proposal by Bhagwati would be difficult to reconcile with the previously described brain gain benefits. Purely from a policy perspective, both measures seem to be rowing in completely different directions. But, beyond this, the coexistence of host-state brain drain taxes and brain gain benefits might well exacerbate the legal problems already suffered by both measures individually.[17] Indeed, both measures are frequently blamed for discriminating regular residents of the host state and new residents after immigration, albeit for different reasons (better treatment of regular residents under host-state brain drain taxes, and better treatment of new residents after immigration under brain gain benefits). It seems apparent that the introduction of a measure (be it a host-state brain drain tax or a brain gain benefit) with a radically opposite purpose to that of the original one (be it again a host-state brain drain tax or a brain gain benefit) would be very unhelpful – actually rather detrimental – in the search of a proper justification or proportion of the described measures. Indeed, it is even harder to justify the different treatment of regular residents of the host state and new residents, whatever it may be, if the opposite policy is promoted at the same time. However, this conclusion proves to be of little value if one takes into account that a host-state brain drain tax has never been implemented, and even if it had been implemented, it is highly unlikely that the jurisdiction would at the same time have passed brain gain benefits. In any case, the proliferation of brain gain benefits is an additional indication of the absolute lack of interest on the part of developed countries in host-state brain drain taxes. However, it would be a huge mistake to extend this incompatibility to any shape of brain drain tax, as we try to demonstrate in the next section.

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[16] This was the version maintained in different papers at least until 1976. For a description of the evolution of the original proposal see Brauner (2010, 240–243).

[17] For more on brain gain benefits, see Section 2 of this contribution; for more on the original Bhagwati tax proposal, see Brauner (2010, 242) and the literature referenced in footnote 134.

3.2. "Brain Drain Taxes 2.0" and Brain Gain Benefits

Even among those most committed to taxing the brain drain, it soon became apparent that a host-state brain drain tax was a dead end.[18] This left no other alternative to a brain drain tax than being levied by the sending (home) state, normally in the form of extended or citizenship-based worldwide taxation. The coexistence of these "brain drain taxes 2.0" with brain gain benefits, as those previously described, must be considered in detail.

3.2.1. Brain drain taxes to the rescue of brain gain benefits

As indicated above, the enormous tax disparities between original residents and inpatriated residents, generated by brain gain benefits in the form of the Spanish special inpatriate regime, might well prove contrary to Constitutional Law constraints. On the other hand, the alleviation of that disparities might frustrate the very purpose of the measure. However, these benefits would not be in the search of justification and proportionality if they were shaped precisely as a way to alleviate excessive taxation generated by the overlapping of the home-state extended residence– or citizenship-based worldwide taxation and the regular personal income tax of the host state.[19] The degree of this alleviation depends of course on the very benefit and the intensity of the home-state brain drain tax, however, whatever this alleviation might mean in practice, it would provide a constitutional justification for brain gain benefits, and particularly a proportionality that they simply do not have in the absence of a home-state brain drain tax. On the other hand, unless all developed jurisdictions in search of skilled immigrants introduce identical brain gain benefits, the "incentive" would maintain its appeal.

3.2.2. Brain gain benefits to the rescue of brain drain taxes

It is quite clear that a home-state brain drain tax, in any of its possible modalities, might generate international juridical double taxation when combined with ordinary residence-based taxation in the host state, assuming that an immigrant will gain residence in the host state immediately upon emigration, according to its domestic law. Although brain gain benefits are not the only way to alleviate this double taxation, as we shall see, they might well serve the purpose of eliminating the most prominent phenomena of double taxation generated by the overlap of

[18] In fact, Bhagwati himself acknowledged that legal restrictions mandated a tax levied by the developing (home) state rather than the developed (host) country. See Brauner (2010, 243).

[19] For the sake of clarity and systematic presentation this excessive taxation will be analyzed in the next section.

national systems induced by brain drain taxes. Different scenarios can be presented regarding this particular issue.

1) In the absence of a double tax convention between the host and the home states.

In this situation the full freedom normally enjoyed by all jurisdictions to define residence criteria will not be limited by a superior rule of law[20] and therefore a situation of double tax residence will be consolidated, which involves, in principle, double taxation on worldwide income. A significant part of this double taxation may be alleviated by the unilateral mechanisms (credits) of the home and the host states,[21] if it exists at all. However, we should not lose sight of the fact that: i) No unilateral mechanism will grant relief for taxes paid in third countries different from the home and the host states. Inasmuch as both countries will tax worldwide income of the migrant, this double taxation will not be relieved. ii) It is very probable that many host (developed) countries will not grant a credit for taxes paid in the home state on the wages gained in the host state. Indeed certain countries will not grant unilateral tax relief for income sourced in their territories, according to their domestic sourcing rules.[22] It is obvious that the wages paid to the migrant in the host state will be sourced in that very state whatever its sourcing rules may be. iii) The frequent petty attitude of states in regard to the application of unilateral tax relief may jeopardize the correction of juridical double taxation in this scenario, as both the host and the home states may fear double credits and end up mutually denying it to the taxpayer.

Brain gain benefits, such as those contained in the Spanish system, will help to alleviate double taxation in the following scenarios: i) if the concerned jurisdictions – particularly the home state – do not have a unilateral mechanism to correct international juridical double taxation, or if it exists, it proves not to be applicable. ii) Inasmuch as the special tax regime implies being taxed just on Spanish-source income it prevents income sourced in third countries – different from the home and the host states – of also being taxed twice by the home and the host states, as states of residence (or the state taxing worldwide income based on citizenship). Of course juridical double taxation, generated by source taxation in a third state and residence or citizenship based taxation in the home state, will depend on the existence of treaties between those states

[20] Unless the freedom to leave a country, envisaged in certain constitutions and international agreements on human rights, is considered a limit in this context.

[21] In this regard see Pomp, Oldman (1979, 36–39).

[22] Although this restriction to foreign tax credit has at times been presented as exceptional there are several countries where foreign tax credit is not recognized for items of income sourced in the residence state. It is a common statement, for example, that foreign taxes imposed on US-sourced income may not be credited (Choi, Rienstra).

and, perhaps more importantly, domestic mechanisms to correct international juridical double taxation.

2) If a double taxation convention exists between the host and the home states.

One might expect that in the presence of a double taxation convention a “brain drain tax 2.0” would not be possible. In fact, in the current international tax regime tax jurisdiction follows residence[23] and it seems certain that the immigrant would gain residence in the host state upon immigration. Additionally, although the home state may expand its residence criteria to also cover emigrated nationals or residents or even develop citizenship-based worldwide taxation, in the presence of an OECD or UN model patterned double taxation convention, the host state will always be the winner in an eventual double residence conflict between the two states. Indeed, the rules contained in Article 4(2) of both the OECD and UN models will normally lead to this result inasmuch as a) the first tie-break rule in the provision (permanent home available) is largely elective[24] – and the immigrant would easily avoid double residence and double taxation altogether; and b) the second tie-break rule – center of vital interests – would lead, at least in our opinion, to decide the residence conflict in favor of the host state .[25]

In the previous context a home-state brain drain tax would be incompatible with the Convention and the brain gain benefits of the host state would lose their justification and therefore, allegedly, their constitutionality. However, two additional scenarios must be considered.

The first is double taxation conventions containing a provision patterned according to the “saving clause” of the U.S. Model Tax Convention.[26] In these treaty circumstances it is obvious that citizenship-based worldwide taxation by the home (sending) state would be in accordance with the corresponding treaty; however, it is also obvious that the overlap of the home-state citizenship-based worldwide taxation and the host-state residence-based taxation might generate double taxation. It is true that – at least according to the current citizenship-based worldwide taxation in the Unites States – a citizen taxed abroad as a resident may

[23] Brauner (2010, 247).

[24] Brauner (2010, 250).

[25] For a different position see Brauner (2010, 250). We will later go back to this question.

[26] According to this provision in the current Article 1(4) of the U.S. Model Tax Convention (2016) “Except to the extent provided in paragraph 5 of this Article, this Convention shall not affect the taxation by a Contracting State of its residents (as determined under Article 4 (Resident)) and its citizens. Notwithstanding the other provisions of this Convention, a former citizen or former long-term resident of a Contracting State may be taxed in accordance with the laws of that Contracting State.”

claim foreign tax credits, in the U.S., for income taxes paid in the residence (host) state.[27] However even if rules similar to the U.S. Foreign Tax Credit were introduced together with citizenship-based worldwide taxation in developing home states, double taxation on income sourced in third countries would persist and brain gain benefits, such as those previously described, would help their elimination at least in regard to worldwide income taxation in both the home and the host states.

The second is double tax conventions with modified tie-break rules. Authors favoring home-state brain drain taxes have claimed a possible variation of tie-break rules contained in Article 4(2) of both the OECD and UN model tax conventions in order to avoid systematic defeats of home (sending) states in double residence conflicts, thereby enabling in practice a home-state brain drain tax based on extended residence of emigrants. The proposal is simply to put the center of vital interests as the tie-break rule before the "permanent home available" criterion, eliminating the elective use of the rule by taxpayers and assuming that during the first years of immigration the center of vital interests remains in the home state.[28] In our view this change would not guarantee the systematic triumph of the home state in possible double residence conflicts. Even if the current Commentaries to the 2017 OECD Model Tax Convention seem to give more weight to the personal aspect of the center of vital interests,[29] it is important to bear in mind that: i) this interpretation has no basis in the wording of the OECD Model which refers to "...the State with which his personal and economic relations are closer (centre of vital interests)"; ii) the assumption that during the first years of immigration the center of vital interests remains in the home state is also questionable. Indeed, economic relations to the host state would be normally greater than those in the home state; on the other hand, it cannot be assumed lightly that all personal ties can be located in the home state. In any case, conflicts of double residence might persist, even under a change of the tie-break rules in the way suggested. Double taxation will arise in such cases, save for the unlikely event that one of the Contracting States relinquishes its claims, assuming the triumph of the other according to a different tie-break rule (normally habitual abode in the host state). This double taxation may proven to be more problematic than in non-treaty scenario, inasmuch as both contracting states might deny correction of double taxation assuming that the other country is not applying the treaty in a correct manner. In this context, the brain gain benefits would serve as a tool to grant partial – yet relevant – relief for this double taxation.

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[27] Kirsch (2007, 504–505).

[28] Brauner (2010, 250).

[29] Article 4 para. 15 of the OECD Model Commentaries states "The circumstances must be examined as a whole, but it is nevertheless obvious that considerations based on the personal acts of the individual must receive special attention."

4. CONCLUSION

The Spanish brain gain benefits special regime, i.e. elective taxation of emigrants in Spain as non-residents during six years after immigration:

1) runs contrary to a traditional host-state brain drain tax increasing the many (legal) problems of the latter and exacerbating the constitutional concerns on the former.
2) may be a perfect complement to home-state brain drain taxes based on citizenship or extended residence inasmuch as: i) the existence of home-state brain drain taxes might well (constitutionality) justify brain gain benefits; ii) brain gain benefits may partially – yet importantly – correct international double taxation connatural to home state brain-drain taxes.

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TAX AND BRAIN DRAIN: JUSTIFICATION, POLICY OPTIONS AND PROSPECT FOR LARGE DEVELOPING ECONOMIES

International migration has continued to escalate over the last three decades, creating a risk of brain drain in developing countries. This paper reviews the extent to which the use of tax instruments to address brain drain can be justified in developing economies with large populations. Furthermore, it explores and assesses tax policy options that may be undertaken to prevent the emigration of high-skilled individual, namely the Bhagwati tax proposal, exit tax, revenue sharing and tax incentives.

Five things can be concluded from the assessment of several policy choices. First, there is no stand-alone tax policy that can optimally address brain drain, in the sense of reducing the number of high-skilled individuals who emigrate. Second, most policies put more focus on the element of fairness to compensate for the "loss" caused by the home country. Third, almost every available policy requires better coordination at the international level. Fourth, all policy options require closer collaboration with immigration agencies. Finally, each policy has the potential to produce unintended consequences.

Key words: *Brain drain. – Large developing economies. – Bhagwati tax. – Exit tax. – Tax incentive.*

1. INTRODUCTION

International migration has continued to escalate over the last three decades. Globalization, ease of immigration procedures, incentives to

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attract talented individuals, and wage inequality between countries act as factors compelling high rates of migration. Nevertheless, one crucial issue lies in international migration, namely the brain drain phenomenon. Brain drain is defined as the transfer of highly skilled human resources from one country to another which disadvantages the migrants' home countries (Gibson, Mckenzie 2011, 3–5).

The brain drain phenomenon is generally experienced by developing countries in which a large proportion of their high-skilled individuals emigrates to developed countries. Limited employment opportunities and the lack of certainty in conducting business have encouraged emigration – in particular, of tertiary-educated individuals – to countries with better wages and economic conditions. Although frequently criticized as one of the causes of the stagnation of economic development in developing countries, some parties are of the opinion that high-skilled migration will lead to benefits for the home country, for instance, the prospect of high remittances, technology transfer, and encouraging investment in education.

As such, how can taxes serve as one of the instruments to prevent the brain drain phenomenon? The role of Jagdish Bhagwati, who more than 40 years ago submitted a proposal considered quite 'advanced' for the time, is crucial to the study on this matter. Bhagwati argues that the home country of high-skilled migrants is expected to receive compensation from the country where the migrants receive income, through a tax scheme to guarantee fairness. Such an idea is then linked to the U.S. citizenship-based tax system. The notion of using tax instruments to prevent brain drain does not stop there. Furthermore, some literature has reviewed various other methods, such as tax incentives to keep high-skilled individuals in the country, exit tax, revenue sharing, and the development of Bhagwati's ideas.

From the standpoint of developing countries, especially those with a large population, the brain drain phenomenon is closely related to the testing of the government's commitment to providing employment opportunities and decent livelihoods for the high-skilled individuals. On the other hand, the movement of high-skilled individuals pertains to the tax base erosion that will, in turn, result in the reduced ability to finance development. In short, the policy dilemma faced by large developing economies is even more complex, and adopting the steps taken by other countries may not prove effective.

As such, to what extent are large developing economies justified in imposing taxes to prevent brain drain? What tax policy choices are ideal for them and what are the implications? This paper will attempt to address these issues.

This paper will review the extent to which apply taxation to address brain drain, in the case of developing economies with large populations,

can be justified, i.e. have strong argumentation. There are four motives why we will chose large developing economies (LDEs) as the focus of this paper. First, from 2000 to 2010, the lower middle-income and low-income country groups saw the highest increase in tertiary-education migration, to nearly double. The greatest risk of brain drain occurs in middle-income countries, especially lower middle-income countries in which almost a third of the tertiary-educated population emigrates abroad. In contrast, in high-income countries, the emigration of the tertiary-educated population can be compensated by the immigration of the tertiary-educated persons from other high-income countries or middle– and low-income countries.

Second, largely populated countries generally face complexity in managing the quality of their human resources and ensuring job opportunities. Third, largely populated countries have a significant influence on the size of brain drain as they play an important role as labor-exporter countries.

Finally, Bhagwati himself states that in the context of developing economies, the impact of brain drain is heavily influenced by the size of the population of a country. For small developing economies, the impact of brain drain is greater. On the other hand, brain drain has no great impact on large developing economies given their large population bases. To address these questions, there must exist a legal standing and benefits for these large developing economies. Furthermore, several available policy options will be reviewed and contrasted with normative tax principles.

This paper will not provide any plenary policy recommendation, instead, will attempt to review the prospects and implications of the various policy choices from the context of large developing economies, among others, the links between exit tax and emigration, the implications of citizenship-based taxation on the principle of non-discrimination, the consistency of developing countries in maintaining the predisposition of the right to tax over source countries, global cooperation, prospects for the use of tax incentives, and so forth.

Within this paper, large developing economies refers to low-income and lower middle-income countries (based on the 2019 World Bank classification) with a large population. The research is limited to countries included in the 20 largely populated countries based on the World Population Database (2019). Of the two criteria, 10 countries are included in this research category, namely: Bangladesh, the Democratic Republic of Congo, Egypt, Ethiopia, India, Indonesia, Nigeria, Pakistan, the Philippines, and Vietnam.

This paper consists of six parts. The first part is the introduction. In the second part, the author reviews the concept, impact, magnitude of the

migration of high-skilled individuals, and its relation to brain drain. An explanation of the economic situations, demographics, human development level, labor situations, and taxation challenges in 10 large developing economies are discussed in the third part, which also addresses the question of whether there exists any justification for large developing economies to impose taxes to prevent brain drain.

The fourth part of this article will examine the justifications for large developing economies to prevent brain drain through tax instruments. This chapter will also explore and assess four tax policy options that may be undertaken to prevent the emigration of high-skilled individuals. The four options are the so-called Bhagwati tax, exit tax, tax incentives to keep working in the country, and revenue sharing. In this article, we argue that by and large there is no optimal stand-alone tax policy. This is discussed in the fifth section, which covers the relation of such policies to tax competition, trends towards citizenship taxation, non-discrimination rule, increasing relevance of the jurisdiction to enforce taxes, and so forth. The sixth part provides a conclusion.

2. INTERNATIONAL HIGH-SKILLED MIGRATION AND BRAIN DRAIN

2.1. Understanding Brain Drain

According to the United Nations (2019), it is estimated that currently more than 270 million people worldwide reside in other countries as immigrants. In an increasingly integrated economy, migration will in due course follow the mobile acceleration of investment flows, trade, and information distribution. Such a trend has turned into a global phenomenon and every government seeks to continue to monitor and sustain its respective national interests. The rising trend of international migration is accompanied by the momentum of differences in demographic structure among countries and the decline in transportation and communication costs (Ozden, Schiff 2006, 2). As such, the fulfillment of labor supply and demands that differ between countries encourages migration. Consequently, preventing migration is increasingly difficult for any country.

Broadly speaking, the availability of the labor force in developed countries was highest in around 2010. Subsequent to the peak, the age dependency ratio of these countries continued to increase. Contrary to this trend, developing countries were heading towards a large labor surplus after 2010, with a declining value of the dependency ratio (Ozden, Schiff 2006, 2). This imbalance results in the demand and supply of labor from these two groups of countries. In normative terms, free mobility

among residents will generate economic efficiency. In addition to benefiting individuals who decide to migrate, there is also additional global productivity (Wamsley, Winters 2005, 690).

Individuals experience such positive impacts too. Since the decision to migrate is based on economic motives, the welfare of individuals also improves. The impact can even extend to the families or people who depend economically on these individuals in the home country, through remittances.

However, an aspect that sometimes escapes attention is the fact that a surplus of labor force availability may not necessarily be followed by a surplus of high-skilled labor. In developing countries with a large population, the need for workers with certain skills is even greater, thus labor has a positive externality to the development of quality and skills of other workforces in general (Grubel, Scott 1966, 273). In addition to aggregate and individual positive economic impacts, there are negative impacts arising from the economic loss of the home country due to the emigration. The absence of human resources that can replace the emigrants' contribution engenders a decrease in productivity in the home country.

In the context of developing countries, this phenomenon should be avoided, i.e. when human resources with certain skills, which may not necessarily experience a surplus, lose such potentials due to migration. As stated by Bhagwati (1976, 3), this is often referred to as brain drain or lack of highly-skilled individuals due to their migration to other countries, which are predominantly more developed.

2.2. Determinant Factors

Based on the perspective of an individual as a rational being, the motives underlying one's decision to migrate to another country are similar to the movement of capital. Given the wide range in wage rates among countries, a person has a different expected income between his home and the host country. Furthermore, these individuals deduct the expected income from the host country by the migration cost. If the result is greater than the current income, there exists a rational motive for the individual to migrate: to obtain economic gain.

Goldin, Cameron, Balajaran (2012, 41) argues that other than economic motives, political and social conditions serve as factors that encourage an individual to move to another country. These are push factors minimized by the home country whereas the pull factors are optimized by the host country.

2.2.1. Push Factors

As aforementioned, low welfare acts as a stimulus for a person to emigrate from their home country. Aspects resulting in such conditions serve as the push factors underlying the decision to change the situation (Elveren 2018, 45). When an individual perceives that the situation in the home country cannot change and thus causes non-optimal well-being, the urge to move abroad becomes stronger.

In general, these aspects cover economic, social, and political factors. According to Docquier (2014, 3–5), the economic factor is triggered by a variety of circumstances, such as inadequate income levels, limited opportunities in the labor market, as well as unstable economic situations or a recession. From a social perspective, possible push factors are cultural incompatibilities with fellow citizens, discrimination, and rejection by the community. On the other hand, possible political push factors are political instability, security, and unideal governance.

For home countries, in particular, developing countries, improving push factors is not an easy task and is time-consuming. Accordingly, regulations incentivized through taxes to discourage and prevent brain drain are applied as the short-term solution. Furthermore, Roudgar (2014, 3) argued some people tend to be impatient and frustrated by unfavorable political, social and economic conditions in the home country. With the expectation that there will be no immediate and significant change, the probability of such people leaving the country will be even greater.

Taxation of brain drain, i.e. by imposing taxes on income for citizens working in host countries in which the collection process is carried out by the host country, although not the most effective solution, is considered an alternative to reducing the pressure of inevitable push factors (Brauner 2010, 45). Nevertheless, as argued by Brauner (2010, 45), this method is deemed ineffective as it requires strong coordination between the home and host countries.

2.2.2. Pull Factors

Furthermore, the realities that act as the push factor in the home country will be rationalized based on the individual's expectations of the situation in the host country. Similar to push factors, better economic opportunities, more stable social and political conditions and compatibility with the culture of the host country will serve as pull factors. In addition to these aspects, tax instruments may also serve as an alternative in incentivizing highly skilled immigrants into the country, for instance, by creating a special tax treatment regime for expatriates with certain skills or working in certain sectors (Roudgar, Richards 2015, 80).

The push factors can be even more intense when the persons have a network of people who can introduce and facilitate them taking advantage of opportunities in the other country. Further, positive experiences from other people who succeed in other countries will incite a person's decision to migrate. Consequently, confidence in the ability to adapt increases.

In anticipation of this, the home country also applies a pull factor strategy targeted at its citizens to minimize brain drain. Improvement of governance, the supply of public goods, and efforts to increase political stability serve as a pull strategy that is generally carried out by the home country (see especially Huntington 1996). Moreover, a special tax regime is applied as a pull effort to invite expatriates back to the country.

2.3. Brain Drain Trend

Overall, almost every country has seen an increase in emigration over time, including in the percentage of the tertiary-educated population (see Table 1). However, from 2000 to 2010, the lower middle-income and low-income groups experienced the greatest increase, nearly doubling.

Table 1. Tertiary-Educated Emigration Based on Countries' Income Group (% Total Emigration)

Income Group Countries	Tertiary-Educated Emigration Rate	
	2000	2010
High-Income	6.3%	8.4%
Upper Middle-Income	14.1%	23.6%
Lower Middle-Income	16.3%	31.8%
Low-Income	8.1%	14.7%

Source: Brücker, Capuano, Marfouk (2013). Education, gender and international migration: insights from a panel-dataset 1980–2010, mimeo. Data is available online at *https://www.iab.de/en/daten/iab-brain-drain-data.aspx* (accessed 8 September 2019)

The greatest risk of brain drain occurs in middle-income countries, especially lower middle-income countries in which almost a third of the tertiary-educated population emigrated abroad. In contrast, in high-income countries, the emigration of the tertiary-educated population can be compensated by the immigration of the tertiary educated persons from other high-income countries or middle– and low-income countries. This is further confirmed by OECD findings, i.e. tertiary-educated persons

commonly emigrate to OECD countries rather than to non-OECD countries (see Table 2)

Table 2. Emigration Rate of Tertiary-Educated Person Based on Country Region and Destination in 2000

Region of Origin	Emigration Rates (% of total emigration)	
	to OECD countries	to Non-OECD countries
World	4.3	1.3
Africa	9.7	1.1
Asia	3.5	0.9
Europe	5.6	2.5
Latin America	7.8	1.1
North America	1.2	0.2
Oceania	7	0.2

Source: Dumont, Spielvogel, Widmaier (2010)

This may be associated with the low prospects of the labor market in developing countries. Various studies show that the increase in the level of education in developing countries may not be in line with better employment opportunities (Guarcello *et al.* 2008). In fact, in Sub-Saharan Africa countries, the highest unemployment rate is found in university graduates (Fan, Stark 2007, 76–87).

In general, as discovered by Ordine and Rose (2011, 582–97), unemployment occurs due to the faster rate of improvement of the education level compared to industrial improvements and the development of employment opportunities that require high skills. Consequently, an imbalance occurs between the availability and requirement of labor .

2.4. Implication

The brain drain experienced by the home country may in part lead to brain waste in the host country as a person with certain abilities from the home country works in the informal sector or performs a job that does not require special skills in the host country, such as a driver, janitor, waiter, and so forth. In other words, brain drain from the home country does not necessarily lead to brain gain in the host country

To sum up, brain drain is to be avoided and anticipated by developing countries. Nevertheless, the research on the implications of

brain drain increasingly shows that the negative impacts are not as severe as formerly expected.

Brain drain should be understood as an event that may not necessarily be permanent (Stark, Helmenstein, Prskawetz 1997, 227–34). The migration of highly skilled workers abroad may be temporary, ultimately returning to their home countries with higher skills. Secondment, training, and education may give rise to migration to a more developed country, leading to "brain investment", which has a positive long-term impact.

Furthermore, brain drain may also be followed by changes in the perception and behavior of a home country towards education and personal development. According to Beine, Docquier, Rapoport (2001, 275–289), with better opportunities abroad, the citizens of the home country will recognize that education has a high return and thus invest themselves and their family members in it. Thus, the brain drain phenomenon can trigger an implicit "brain gain" that would not be obtained without the opportunity to migrate abroad (Docquier, Rapoport 2007, 15–16). The positive impact on education and skills ultimately results in a multiplier effect, improving the overall benefits for the country.

Ultimately, the estimated impact of brain drain cannot be separated from the impact of brain gain due to the migration. Thus, the impact to be considered is the difference between the two, which may take the form of net brain drain or net brain gain.

3. LARGE DEVELOPING ECONOMIES: AN OVERVIEW

3.1. Context

In this article "developing economies" refers to the World Bank's classification as of June 2019, concerning low-income and lower middle-income countries. The countries in the two categories are classified as developing economies since they commonly emit migrants and yet are not preferred emigration destinations for residents of other countries. Thus, in net terms, these countries have higher emigration than immigration rates. Therefore, their interest in the issue of brain drain is significantly more relevant. Furthermore, the World Bank classifies low-income and lower middle-income countries as having a gross national income (GNI) per capita amounting to less than USD 3,996 per capita in 2018 (World Bank 2018).

On another note, the term "large" refers to countries with large populations. There are three underlying reasons why the term "large" is

used in this context. First, largely populated countries generally face complexity in managing the quality of their human resources and ensuring job opportunities. Second, largely populated countries have significant influence on the size of brain drain. Finally, as stated by Bhagwati, migration of high-skilled individuals should not have much impact on large developing economies.

This paper reviews 10 large developing economies as case studies. The population data used is from the World Population Prospect, published by the United Nations Population Division. Generally speaking, these 10 countries were selected to provide an overview of the issues and situations in large developing economies and not intended to specifically establish solutions for each country. The ten countries are as follows: Bangladesh, the Democratic Republic of Congo, Egypt, Ethiopia, India, Indonesia, Nigeria, Pakistan, the Philippines, and Vietnam. The population of these 10 countries stands at 2.68 billion, i.e. 35.3% of the world's population.

3.2. Economic Situation

This section discusses the economic structure of the 10 selected large developing economies (LDE). Some of the economic indicators discussed are the performance of Gross Domestic Product (GDP), demographics and labor conditions, and the quality of human development.

3.2.1. Gross Domestic Product[1]

Based on its economic growth, Ethiopia is the country with the highest economic growth among the 10 sample countries. Based on the sectoral contributions to the GDP, this country relies heavily on agriculture, which accounts for 30% of the GDP. In 2014 its economic growth was more than 10%. However, this figure decreased to 6.8% in 2018, dropping approximately 3% compared to the previous year. One of the factors resulting in Ethiopia's high economic growth is the state's investment in the public sector, primarily in developing social and economic infrastructure. Further, the government intervenes in the rural economy, specifically in the agricultural sector (Seid, Alemanyehu, Seid 2016, 5).

Three other countries that show satisfying economic growth performance are Bangladesh, Vietnam, and India. Bangladesh is the world's second-largest textile exporter and is slowly reducing its dependence on imports and foreign aid. Bangladesh's GDP growth is quite satisfying, experiencing an upward trend, ranging from 6% to 8% in the past five years, i.e. from 2014 to 2018.

[1] Data and information related to economic growth performance in this section (Gross Domestic Product (GDP) growth and sectoral contributions (agriculture, services, manufacturing, and mining) to GDP are sourced from the World Development Indicators – World Bank Group.

On the other hand, Vietnam's economic growth in 2018 reached 7.1%. This growth was driven by foreign investment, triggered by various policies favoring foreign investors. One of the policy mechanisms applied by the Vietnamese government is to completely open access to ownership of several domestic companies to foreign parties. The purpose of such a policy is to reduce the level of corruption and increase efficiency. However, ownership of shares in several sectors such as banking, telecommunications, aviation, and defense remains restricted (Jennings 2017). Additionally, the contribution of the manufacturing and service sectors to Vietnam's total GDP is sustainable despite the downward trend in the agriculture and mining sectors.

India, a neighboring country of Bangladesh, has an economic growth pattern that tends to be stable at around 7%. As a matter of fact, its economic growth in 2016 amounted to 8% but again declined in subsequent years. Slower post-2016 GDP growth may have stemmed from temporary disruptions in the economy. Two policies that resulted in the shock were the implementation of fiscal reform through the Goods and Services Tax (GST) and monetary reform through demonetization (World Bank 2018). Two other countries in the ASEAN Region, Indonesia and the Philippines, had stable economic growth in the range of 5% to 6% from 2014 to 2018. Pakistan also saw a similar economic growth rate even though the three countries have relatively different sectoral contribution patterns. Pakistan itself depends on the agricultural sector. In contrast, the majority of Indonesia's and the Philippines' GDP originates from the manufacturing sector.

Furthermore, the Democratic Republic of the Congo (DRC) and Nigeria tend to have a uniform pattern of economic growth. The two countries on the African continent managed to recover from the downward trend in GDP growth between 2014 and 2016. The DRC itself is a country that is highly dependent on the mining sector in its economic structure. The country's economic growth reached 6% in 2018, whereas in 2016 it stood at only 2.4%. Such a fact is inseparable from political and security conditions that have stabilized, which greatly affects economic activity (The Heritage Foundation 2019).

Nigeria managed to recover from a previously negative GDP growth, in 2016, to positive growth the following two years. A worldwide drop in oil prices, together with low foreign exchange revenue from the non-oil sector, resulted in low and decelerating economic growth in 2016, according to World Bank (2017). Egypt, another African country, has relatively low economic growth. It's GDP growth in 2014 only stood at approximately 3% and increasing to 5.3% in 2018. This is inextricably linked to the economic reform program carried out by the Egyptian government, relying on cooperation with the International Monetary Fund (IMF) since 2016 (IMF 2018).

3.2.2. Demographics and Labor

The identification of demographic and labor conditions with regard to brain drain can be traced through the age dependency ratio. In simple terms, the age dependency ratio can be defined as a comparison of the number of people who are of the non-productive age and those of the productive age.

World Bank data shows that the DRC is the country with the highest dependency ratio, 97%. This value shows that for every 100 productive age persons in the DRC, 97 residents depend on the productive age population. On the other hand, Vietnam places last, with a ratio of 44%, which that does not even amount to half of the DRC's.[2] Nonetheless, the dependency ratio alone is insufficient to assess a country's economic conditions as it only indicates the size of the productive age population, regardless of whether it is employed. Thus, attention should be focused on other labor-related indicators.

Table 3. Age Dependency Ratio and Unemployment Rate in Selected Large Developing Economies (2018)

LDE Countries	Dependency Ratio (% of working age population)	Unemployment Rate (% of labor force)
Bangladesh	49	4.3
DRC	97	4.2
Egypt	64	11.4
Ethiopia	79	1.8
India	50	2.6
Indonesia	48	4.3
Nigeria	87	6.0
Pakistan	66	3.0
The Philippines	56	2.5
Vietnam	44	1.9

Source: World Bank (2019)

[2] The World Bank's version of the age dependency ratio is the total population under the age of 15 years and over 64 years compared to the population aged between 15 and 64 years, which is considered the working-age population. Source: *https://data.worldbank.org/indicator/SP.POP.DPND.*

Based on World Bank unemployment data, Egypt is the country with the largest unemployment rate, i.e. roughly 11.4% in 2018.[3] This value is significantly higher than in the DRC, where the unemployment rate is only 4.2% in 2018, even though the dependency ratio was significantly higher than in Egypt. Thus, it can be implied that employment opportunities in Egypt are relatively low compared to its sizeable productive population. A low dependency ratio along with high unemployment may lead to emigration, particularly, for individuals of productive age, regardless of their level of education and skills. The comparison between the dependency ratio and the unemployment rate can be seen in the Table 3.

Table 3 shows the dependency ratios in the ten countries. Based on the information, India, Bangladesh, Indonesia, and Vietnam have demographic advantages compared to other LDE countries where the productive age dominates the population (demographic dividend).

3.2.3. Human Development Level

The factor that determines the economic development of a country is not only its economic growth but also the quality of human resources (HR), assessable through the Human Development Index (HDI). The HDI indicator itself is an assessment of the dimensions of human development which is subsequently normalized by a geometric index, which is estimated.

The dimensions of human development estimated in the HDI are health, knowledge, and economics. The health dimension contains indicators in the form of life expectancy for a country's population. In contrast, the dimension of knowledge is estimated through the length of education and the proportion of people attending school. Furthermore, the economic dimension that shows the quality of human resources is estimated using the Gross National Income (GNI) per capita.

Based on estimates conducted by the United Nations Development Program (UNDP), none of the LDE included in this study achieved the ranking of very high or high human development country in 2017. The Philippines ranked 113th, the highest in the HDI ranking, followed by Egypt (115), Indonesia and Vietnam (116), India (130), Bangladesh (136), and Pakistan (150) which were classified as medium human development countries. The other three countries are categorized as low human development countries, namely Nigeria, Ethiopia, and the DRC, ranked 157th, 173rd, and 176th, respectively.

[3] The World Bank's version of unemployment data pertains to the number of unemployed people who are actively looking for work compared to the total workforce. Source: *https://data.worldbank.org/indicator/SL.UEM.TOTL.ZS.*

The HDI score is also supported by information pertaining to the portion of the population that has completed education up to the secondary level (equivalent to high school) and tertiary (equivalent to university).[4] The Philippines has a relatively high school enrolment rate for secondary and tertiary education, around 89% and 35% respectively. In contrast, the DRC, the country with the lowest HDI, has the lowest number university graduates, only 7%.

3.3. Brain Drain: Magnitude of the Problem

This section identifies some patterns and trends causing emigration in LDE countries, with a view to establishing the right measures in formulating policy priorities related to the taxation of brain drain. These factors include migration patterns as well as economic contributions to the home country.

3.3.1. International Migration Pattern

It is recommended that developing countries with satisfactory economic development to observe the pattern of emigration by their citizens, to allow for the mapping in any country that has the potential for brain drain. One possible indicator is the classification of the level of education of emigrating citizens.

Having observed the role of human resources quality, which significantly determines the economic development of a country, we can now map patterns of population emigration from LDE countries to developed countries. This mapping can serve as an indicator of the extent of access that developed countries provide to emigrants from various developing countries, based on their level of education. Additionally, this mapping can also show the determinant factors of emigration in regard to the economic development potential of the home country.

Table 4. The Proportion of Emigrants Migrating to 20 OECD Countries by Education Level

Home country	2000			2010		
	Low	Medium	High	Low	Medium	High
Bangladesh	57.9%	11.5%	30.6%	43.8%	15.2%	40.9%
Congo, Democratic Republic	38.1%	27.1%	34.8%	32.8%	28.2%	39.0%

[4] The data used is sourced from the World Bank relating to school enrolment per capita level, available at: *https://data.worldbank.org/indicator/SE.SEC.ENRR* for secondary education level, and *https://data.worldbank.org /indicator/SE.TER.ENRR* for tertiary education level.

Home country	2000			2010		
	Low	Medium	High	Low	Medium	High
Egypt	20.1%	23.4%	56.5%	14.6%	22.8%	62.6%
Ethiopia	23.9%	32.7%	43.5%	16.6%	33.3%	50.1%
India	30.1%	12.8%	57.1%	19.4%	12.0%	68.6%
Indonesia	34.0%	25.4%	40.6%	27.3%	24.0%	48.7%
Nigeria	19.9%	16.6%	63.4%	14.2%	15.4%	70.4%
Pakistan	50.5%	14.5%	35.0%	37.2%	15.9%	46.9%
The Philippines	13.4%	21.2%	65.4%	9.1%	18.8%	72.1%
Vietnam	36.8%	27.9%	35.3%	30.3%	28.2%	41.5%

Source: Brücker, Capuano, Marfouk (2013). Education, gender and international migration: insights from a panel-dataset 1980–2010, mimeo.[5]

Based on data on emigration to various developed countries as shown in Table 4, the proportion of tertiary-educated emigrants to developed countries has a growing trend. On the other hand, the number of secondary-educated emigrants migrating to developed countries has a decreasing trend. This indicates the potential for brain drain that actually benefits developed countries amid their slow population growth, supported by various types of pull factors that were formerly available.

In addition to the pattern of emigration to developed countries, we need to observe which are the citizens with high levels of education that emigrate the most. This may point to the country's push factors with the potential to cause brain drain. Table 5 shows the number of emigrants from 10 LDE countries throughout the world.

Table 5. Tertiary-Educated Emigration on Selected Large Developing Economies

Country	1975	1980	1985	1990	1995	2000	2010	
							Male	Female
Bangladesh	1.8%	1.7%	2.0%	1.8%	3.1%	4.0%	3.6%	3.6%
Congo, D.R.	8.2%	7.7%	8.2%	8.0%	8.3%	7.6%	15.5%	7.1%
Egypt	7.5%	5.9%	7.5%	5.4%	4.4%	4.1%	3.1%	3.9%

[5] Source: *https://www.iab.de/en/daten/iab-brain-drain-data.aspx* (accessed September 8, 2019).

Country	1975	1980	1985	1990	1995	2000	2010	
							Male	Female
Ethiopia	1.5%	2.1%	4.9%	7.1%	8.3%	9.2%	N/A	N/A
India	2.9%	3.2%	2.7%	2.8%	3.1%	4.2%	4.1%	3.1%
Indonesia	3.3%	5.6%	8.3%	2.6%	1.9%	1.3%	2.8%	2.2%
Nigeria	2.2%	2.1%	4.3%	7.7%	9.3%	10.1%	N/A	N/A
Pakistan	2.7%	5.4%	6.7%	6.5%	9.5%	12.0%	6.9%	6.0%
The Philippines	9.9%	9.5%	10.9%	12.5%	12.1%	13.2%	9.6%	6.2%
Vietnam	16.1%	17.1%	26.2%	23.9%	25.2%	26.3%	10.9%	10.1%

Source: 1975–2000 data is from Cecily Defoort, Tendances de long terme en migrations internationales: analyse à partir de 6 pays receveurs, Manuscript in French, Université Catholique de Louvain. (2006); 2010 data is from Barro and Lee (2013) as quoted in Arslan (2016, 26–29).

On closer inspection, the potential for brain drain is greatest in countries in the South Asian region. Countries such as Bangladesh, India, and Pakistan have experienced a significant rise in the emigration of the population with a tertiary education level, compared to the total number of the countries' emigrants. Meanwhile, the emigration of people with a high level of knowledge decreased in the DRC and Indonesia. Other countries, such as Egypt, Ethiopia, Nigeria, the Philippines, and Vietnam have experienced moderate increases in emigration of this population. Finally, in the case of LDE countries, pull factors seem to be more significant than push factors in causing brain drain of individuals with high levels of education.

3.3.2. Remittances

Public debate generally infers that brain drain only benefits developed countries. In contrast, several parties suggest that this phenomenon could also contribute to the level of welfare of people in developing countries. One quantifiable consequence is the remittances from the diasporas.

Based on World Bank estimates in 2018, the ten LDE countries generate more than 36% of remittances from all over the world.[6] India, the Philippines, and Egypt are three of the top countries receiving remittances, with revenues of US$ 79 billion, US$ 34 billion, and US$ 29 billion respectively. However, the remittances received by India are relatively low compared to its GDP, as shown in Table 6.

[6] Source: *https://data.worldbank.org/indicator/BX.TRF.PWKR.CD.DT.*

Table 6. Comparison of International Remittances to GDP

Country	Remittance (% GDP)
Bangladesh	5.7%
Congo, Dem. Rep.	3.8%
Egypt, Arab Rep.	10.2%
Ethiopia	0.5%
Indonesia	1.1%
India	2.9%
Nigeria	6.1%
Pakistan	6.8%
The Philippines	10.2%
Vietnam	6.5%
Total 10 Countries	4.0%

Source: World Bank (2019)

According to Kapur (2004, 16), remittances alone can be a relatively stable source of external financing, especially for developing countries. Moreover, co ceptually, remittances may have a positive impact on the economy of the recipient country. Remittances to recipient countries in the form of international remittances can contribute to the country's long-term savings and investment. According to Solimano (2013, 15), in the short run, this may lead to positive effects on aggregate demand and output through consumption by individual recipients in the home country.

3.4. Tax Situation

This section provides a review of the tax system, on a macroeconomic scale, relating to the contribution of tax revenue. Data on tax contributions to the economy, both in the form of the tax ratio and the tax revenue structure, is sourced from the World Bank,[7] the OECD,[8] and other

[7] The World Bank data used in this article is available at *https://data.worldbank.org/indicator/gc.tax.totl.gd.zs* (tax ratio), *https://data.worldbank.org/indicator/GC.TAX.GSRV.RV.ZS* (VAT revenue against total tax revenue) and *https://data.worldbank.org/indicator/GC.TAX.YPKG.RV.ZS* (corporate and individual income tax revenues against total tax revenues).

[8] The data on the tax ratio and revenue per type of tax against total tax revenue from OECD is sourced from the OECD Global Revenue Statistics Database, which can be

national sources. Furthermore, this section reviews tax regimes relating to the system of taxation of individuals in general, expatriates residing in these countries (inward expatriates), and the citizens of those countries who emigrate abroad.

3.4.1. Bangladesh

Bangladesh's tax ratio was recorded at 8.8% in 2016. According to World Bank (2019), in terms of the tax structure that same year, 25.2% of the total tax revenue was raised from income tax, while 32.3% of the total tax revenue was from VAT. Regarding taxation on individual income, the Bangladesh government taxes the worldwide income of residents, i.e. if a resident receives income outside the territory of Bangladesh, it will still be subject to taxation. On the other side, non-resident individuals are liable to tax on income received in Bangladesh regardless of where the income is generated. The tax rate ranges from 0% to 30%, with six income brackets.

A person is deemed a resident if residing in Bangladesh for 182 days or more in the fiscal year concerned. Furthermore, a person will also be considered a Bangladeshi resident if he resides for 90 days or more for the year in which the income concerned is generated if the person has previously stayed for more than 365 days in the span of four years prior to the fiscal year concerned.

Income from expatriates working on foreign aid projects established under an agreement between the Government of Bangladesh and a foreign government is exempt from taxation. Additionally, the government provides deduction for expatriates working in the field of technology. Following Ahmed (2019, 12), foreign technicians working in companies registered in Bangladesh and located in special economic zones, or the Bangladesh Hi-Tech Park area, involved in the procurement of goods and services, will receive 50% income tax relief for period of three years. No specific tax regime exists for non-resident Bangladeshi nationals.

3.4.2. Congo, Democratic Republic of (DRC)

The DRC's tax ratio in 2016 stood at 7.6%. This state tax revenue is supported by VAT, which reached 32.7% of the total tax revenue that same year. Furthermore, personal and corporate income tax revenues amounted to 15.8% and 14.5% of the total tax revenue, respectively (OECD 2018). For individual income tax, the DRC government taxes the "territorial" income of residents. In other words, if a DRC resident earns income outside the DRC territory, their income is not subject to tax. The

accessed via: https://stats.oecd.org/Index.aspx?DataSetCode=REV. The codes used are 1000 for Corporate Income Tax, 1100 for OP Income Tax, and 5110 for VAT.

tax rate ranges from 0% to 40%, with ten income brackets. A person is deemed as a resident if they reside in the DRC for more than six months during the given fiscal year.

Due to taxation on individuals' territorial income, expatriates are subject to the generally applicable employee income tax. Other remunerations paid to expatriates are subject to a special tax called the Exceptional Tax on Expatriate Remunerations. According to Kating (2019, 8), this special tax is imposed on employers. No specific tax regime exists for non-resident Congolese nationals.

3.4.3. Egypt

Egypt's tax ratio in 2016 was recorded at 15.2%. The personal income tax revenue accounted for 10.8% of the total tax revenue. Furthermore, VAT revenue raised 18.1% to the total tax revenue. The tax revenue was dominated by corporate income tax, which accounted for 31.9% of the total tax revenue (OECD 2018).

Regarding taxation on individual income, the Egyptian government taxes the "worldwide" income of residents. The tax rate ranges from 0% to 22.5%, with five income brackets. A person is classified as a resident if they reside in Egypt for more than 183 days during the given fiscal year and have permanent residence in Egypt. Furthermore, a person of Egyptian nationality who is domiciled abroad, but still earns income from Egypt, is also be considered a resident and subject to individual income tax by the Egyptian tax authority. There is no special tax treatment for expatriates. In other words, foreign nationals will receive the same treatment as Egyptian citizens. No specific tax regime exists for non-resident Egyptian nationals. (Hamzaoui 2019, 8).

3.4.4. Ethiopia

Ethiopia's tax ratio in 2017 stood at 7.6%. Corporate and individual income tax accounted for 29.7% of the tax revenue that year, with VAT contributing 33.3% (World Bank 2019).

In terms of taxation on individual income, the Ethiopian government taxes the "territorial" income of residents. The tax rate ranges from 0% to 35%, with seven income brackets. A person is classified as a resident if they reside in Ethiopia for more than 183 days during the given fiscal year. The income of foreign professionals recruited to transfer knowledge related to investment in exports is entitled to a tax exemption for a maximum of five years, under directives issued by the Minister (Lencho 2019, 10). No specific tax regime exists for non-resident Ethiopian nationals.

3.4.5. India

India's tax ratio in 2017 was 11.2%. In that year, India's corporate and personal income tax contributed 44.2% to the total tax revenue. Furthermore, the share of VAT revenue in the total tax revenues reached 31.5%. (World Bank 2019)

Regarding taxation on individual income, the Indian government taxes the "worldwide" income of residents. The tax rate ranges from 0% to 30%, with four income brackets. A person is classified as a resident if they reside in India for a minimum of 182 days during the fiscal year. Further, individuals residing in India for 60 days in the given fiscal year, with a record of staying at least 365 days within the four years prior to the given fiscal year will also be classified as residents.

Income paid to expatriates working in India is treated as income sourced in India and taxed according to the applicable provisions in India. Costs of living and travel expenses and remuneration may be granted tax breaks. Tax relief for remuneration given to foreign employees working in foreign companies is highly dependent on certain conditions, including not exceeding the domicile period within India and not making claims for tax deductions that may reduce the tax payable on income (Shah 2019, 10). No specific tax regime exists for non-residents of Indian nationals.

3.4.6. Indonesia

Indonesia's tax ratio in 2017 was 11.5%. According to the Ministry of Finance of Indonesia (2019), the share of tax revenue in the total revenue was 10.1% for personal income tax; 19.2% for corporate income tax; and 39.6% for VAT for the year.

In terms of taxation on individual income, the Indonesian government taxes the "worldwide" income of residents. The tax rate ranges from 5% to 30%, with four income brackets. A person will be classified as a resident if they reside, possess a work visa, a work contract, have a business and other activities in Indonesia for more than 183 days in the given fiscal year.

The tax authority can make adjustments to the amount of income earned by a foreign employee under the guidelines for salaries/wages of foreign nationals, if the income is not supported by proper documents. Also, expatriates' income is deemed as taxable income in Indonesia. This can occur if the expatriate is seconded to a local company by a foreign company where the local company subsequently relocates the expatriate's income in the form of payments (for example, management, technical, or other service costs) to a foreign company (Koo 2019, 8). No specific tax regime exists for non-resident Indonesian nationals.

3.4.7. Nigeria

Nigeria's tax ratio is classified as very low and based on the country's tax authority data, tax revenues only stood at 3.4% and 4.8%, in 2016 and 2017 respectively. However, these figures were up compared to the 2013 tax revenue of 1.5% of the total GDP. Furthermore, in 2013 the VAT only amounted to 0.1% of GDP, i.e. around 9.5% of the total tax revenue, while more than 80% of tax revenue was contributed by corporate income tax.[9]

As for individual income taxation, the Nigerian government taxes the "worldwide" income of residents. The tax rate ranges from 7% to 24%, with six income brackets. A person is classified as a resident if residing in Nigeria, staying for more than 183 days in a period of 12 months or serving as a Nigerian diplomatic agent outside Nigeria. There is no special expatriate tax regime nor special tax treatment for non-resident Nigerian nationals (Odimma 2019, 8).

3.4.8. Pakistan

Pakistan's tax ratio for the fiscal year 2017, namely from July 2016 to June 2017, was 12.5% (World Bank 2019, 1). Based on data from local tax authorities, the structure of tax revenue in the same fiscal year was supported by indirect tax revenue which contributed more than 60% of the total tax revenue. The revenue from VAT, which is an indirect tax, amounted to 39.9% of the total tax revenue. Furthermore, the direct tax revenue or income tax revenue amounted to 39.9% of the total tax revenue.[10]

Regarding taxation on individual income, the Pakistani government taxes the "worldwide" income of residents. The tax rate ranges from 0% to 29%, with eight income brackets. A person is classified as a resident if they stay in the country at least 183 days in the given fiscal year. Furthermore, civil servants assigned abroad are considered residents.

The income of expatriates with resident status but sourced from outside Pakistan are entitled to a tax exemption if their domicile period in Pakistan does not exceed three years. Nonetheless, the tax relief does not apply if the expatriate's income is sourced from companies established in Pakistan or if the income from overseas is brought in or received by expatriates within Pakistan. As demonstrated elsewhere (Koo, Bukhari 2019, 12), foreign income from expatriates returning to their home countries is exempted for four years after the year they left Pakistan. No specific tax regime exists for non-resident Pakistani nationals.

[9] Source: IMF Government Finance Statistics, available at: *https://data.imf.org/?sk=FA66D646–6438–4A65–85E5-C6C4116C4416*.

[10] Source: Federal Board of Revenue of Pakistan available at: *http://www.sbp.org.pk/ecodata/tax.pdf*.

3.4.9. The Philippines

The Philippines' tax ratio in 2017 was 17.5%. In 2017, the structure of this state tax revenue was sustained by corporate income tax with its share amounting to 24.5% of the total tax revenue. Furthermore, the individual income tax and VAT contributed 14.1% and 13.2% of the total tax revenue, respectively (OECD 2019).

In connection with taxation on individual income, the Philippines government taxes the "worldwide" income of residents. The tax rate ranges from 0% to 35%, with six brackets based on income. A person is subject to individual income tax if they holds citizenship or are an alien individual. Additionally, all citizens are categorized as residents except in cases where they meet the criteria for non-residents.

Citizens and foreigners employed at regional headquarters, regional operations headquarters, foreign banking units, and oil service contractors or subcontractors located in the Philippines are subject to a 15% final tax on gross income. Foreigners who are considered as alien individuals are deemed equal to citizens. Furthermore, there is an immigration tax for individuals who enter the Philippines and stay for more than 60 days (Ocampoo 2019, 12). Currently, no specific tax regime exists for non-resident Philippine nationals, however, until the end of the 1980s the Philippines taxed its citizens on all of their income (see Pomp 1985).

3.4.10. Vietnam

Vietnam's tax ratio is relatively high. In 2015, tax revenues reached 18% of total GDP revenues. The highest share of tax revenue that year was from VAT, which accounted for 33.3% of the total tax revenue, i.e. approximately 6% of the GDP. Corporate income tax and the individual income tax revenues accounted for 25% and 7% of the total tax revenue, respectively (IMF 2018, 33).

As for individual income taxation, the Vietnamese government taxes the "worldwide" income of residents. The tax rate ranges from 5% to 35%, with seven income brackets. A person shall be deemed a resident if they stay for 183 days or more in the given fiscal year, starting from the date of arrival. Otherwise, a person whose residence is registered as a permanent home or a rental house with proof of a particular contract is also classified as a resident.

Non-residents are taxed at a flat rate of 20% on employment income sourced from the territory of Vietnam, without any tax deductions. As reported by Grunkorn, Do, Nguyen (2019, 7–8), however, a 50% tax deduction is granted to foreign experts working on the Official Development Assistance (ODA) projects. No specific tax regime exists for non-resident Vietnamese nationals.

4. JUSTIFYING TAX TO ADDRESS BRAIN DRAIN AND POLICY OPTIONS

4.1. Justification to Use Tax Instruments

Based on research related to the economic situation, demographics, human development levels, and the tax system in 10 LDEs, there exist at least four preliminary conclusions, in addition to the high-skilled migration patterns.

First, the 10 LDEs in this article have relatively varied economic developments. This is demonstrated by the growth and structure of their GDPs. However, other than having generally low per capita income, the contribution of the traditional sector is great and mostly from the agriculture sector. There are socio-political factors that distort the economy as well. Second, the level of human development generally features a fairly low human development index (2018). Specifically, for the education sector, variations in the level of education in the ten countries are still relatively low if observed based on the number of human resources with tertiary education level. Another interesting aspect is the tendency that the level of education correlates with the familial economic background. A person who comes from a wealthier family tends to have the ability to undertake tertiary education (Darvas, Gao, Bawany 2017, 25).

Third, given the large population, more significantly, the challenge faced by large developing economies is to ensure the availability of jobs. Interestingly, four out of the 10 countries examined in this article are in (or heading in the direction of) the demographic dividend phase, where the size of productive-age population will be greater than the non-productive-age population. The demographic dividend can certainly be utilized to increase the economic thrust if and only if employment is sufficiently available, otherwise unemployment is likely to escalate. Another noteworthy phenomenon is the rise of the educated unemployment – the labor force that does not have jobs but has tertiary education.

Fourth, the performance of tax revenue in these countries is for the most part relatively weak. This is indicated by the tax ratio, which ranges from less than 5% (Nigeria) to more than 15% (the Philippines and Vietnam). Gaspar, Jaramillo, Wingender (2016, 30) estimates that a tax ratio of 15% is the tipping point for growth stability.

The challenges faced by these countries generally stem from the informal economy, illicit financial flow, corruption in the tax sector, as well as tax revenues that are dominated by corporate income tax and certain sectors. Their performance is insufficient, especially for individual taxation. Individual income tax treatment for migrants generally refers to

the concept of residence, i.e. taxing income sourced from within and outside the country. Broadly speaking, citizens who are not categorized as residents (who reside and earn income abroad) are not taxed.

All the above-mentioned conditions are factors to be considered in discussing whether using tax instruments to prevent brain drain can be justified. Again, what we refer to as justification in this paper is the reasoning or argumentation, not merely the terms to have personal or economic attachment, in the context of international taxation.

4.1.1. Brain Drain or Brain Gain?

The debate about the costs and benefits of high-skilled migration is not something new. Although this phenomenon is often deemed as a loss for developing countries, because emigration makes it difficult for developing countries to achieve economic growth, there is also contrary opinion.

Emigration opportunities may serve as a solution to the availability of jobs. The economy of developing countries, which is quite dominated by the traditional sector, has resulted in employment for labor force with a higher education background. The data in Table 5 shows that emigrants from the 10 LDEs in this article are dominated by emigrants with tertiary education levels.

This strongly indicates the existence of labor opportunity and a relatively higher wages level for workers with tertiary education in developed countries, specifically the OECD. A similar pattern also exists in the case of unskilled labor. Employment opportunities abroad indirectly support developing countries in reducing unemployment, increasing foreign exchange, and reducing the possibility of social unrest. This seems to be the case in Indonesia which routinely sends low-skilled labor to Malaysia, Hong Kong, and Saudi Arabia.

Another strong argument pertains to emigration activities related to remittances. Remittances sent by high-skilled migrants are considered able to address liquidity problems, reduce poverty, catalyze technological adaptation, and stimulate investment in education. However, (Docquier, Rapoport 2011, 27) found that the effect of remittance is strongly influenced by the amount remitted by emigrants and the impact of its distribution in the home country. On a side note, the remittances received by 10 LDEs in this article amounted to USD 228.6 billion in 2018, which is far greater than the global value of official development assistance (ODA), which stood at only USD 162.8 billion.[11]

[11] Global position in 2017. On a side note, net official development assistance (ODA) consists of disbursements of loans made on concessional terms (net of repayments of principal) and grants by official agencies of the members of the Development Assistance

In sum, why should high-skilled migration be taxed if it benefits the home country?

4.1.2. Motivation to Emigrate

Individual motivation to emigrate from developing countries is basically influenced by push and pull factors, as well as tax and non-tax motives. Empirical studies on the causes of emigration have shown various patterns, for instance, the high level of emigration of medical personnel from Africa is largely driven by pull factors, such as better salaries and livelihoods, while the dominant push factor is solely caused by the risk of contraction of HIV.

Interestingly, there is little argument that tax is one of the push factors for emigration decisions for high-skilled individuals. As reported in Kauppinen, Ropponen (2018), there are only a few empirical studies on this matter. On the one hand, this confirms that taxes are indifferent towards an individual's migration to another country. On the other hand, non-tax related matters are more likely to have the most significant impacts.

In terms of pull factors, we should be aware that developed countries strive – driven by the aging population problem and intended to boost the domestic economy – to attract new talents from around the world to migrate to their countries.

Avi-Yonah (2015, 45–56) presents a noteworthy argument: efforts to reduce tax burdens are presently possible if capital mobility is followed by the transfer of resident status, especially in the increasingly transparent tax landscape due to the automatic exchange of information cooperation. However, both elements – incentives and tax planning – are more relevant in non-tax compliance practices of high net-worth individuals (HNWI) and not in the context of brain drain.

The next question is can taxation be justified, if the tax factor is indeed a less-dominant factor in the decision to emigrate. Should the causal factors of the emigration be addressed instead?

With respect to public finance, fiscal instruments – taxes among others – have tasks that include allocation, distribution, and stabilization. In terms of their role in allocating the most efficient resources, taxes are

Committee (DAC), by multilateral institutions, and by non-DAC countries, to promote economic development and welfare in countries and territories on the DAC list of ODA recipients. It includes loans with a grant element of at least 25 percent (calculated at a rate of discount of 10 percent). Sources: Development Assistance Committee of the OECD, Geographical Distribution of Financial Flows to Developing Countries, Development Co-operation Report, and the International Development Statistics database, available at *https://data.worldbank.org/indicator/DT.ODA.ODAT.CD.*

intended to change the behavior of economic agents, among others, creating disincentives for high skilled individuals to emigrate.

4.1.3. Tax Burden and Redistribution

In a closed economic system, skilled and unskilled individuals are subject to domestic income taxes. In the context of ensuring income redistribution and preventing inequality, the individual income tax system will generally be designed progressively. This implies that a person with a higher income or a higher ability to pay will face a higher tax burden (vertical equity). It is worthy of note that the income received by a person is affected by skills and educational background, among other factors. The higher a person's education, the greater the possibility for them to obtain a position with relatively satisfactory returns/wages. Hence, the returns obtained by skilled individuals are in general far better than those by unskilled individuals.

On the other hand, in an open economy where individuals can migrate (particularly if perfect individual mobility exists), a skilled individual can choose a country where their income and welfare will be much better. In such cases, the tax system is ultimately unable to redistribute income fairly.

In turn, the tax system – which is intended to create fairness – will result in a higher tax burden for a high-skilled individual who remains in the home country. A higher tax burden and the opportunity to emigrate will encourage domestic high-skilled individuals to emigrate and result in a revenue loss (see, for example, Bhagwati and Hamada 1982). The state is ultimately pressured to restrict emigration by reducing the tax burden on high-skilled individuals (with a higher ability to pay). Consequently, this leads to a less egalitarian or unfair tax system. Further, the loss of the tax base (due to emigration) and the need for significant development funds will simultaneously increase the tax burden for individuals "left behind" in the home country.

It is true that individual mobility across-country can lead to a more efficient provision of public goods and services. However, this also limits the country's ability to distribute income fairly as hypothesized by Tiebout (1956, 417) in the context of sub-national taxes. Additionally, Wilson (2011, 75) also reports that immobile residents bear the burden of taxation due to the high emigration rate of high-skilled individuals. Hence, a tax on brain drain can ensure that the redistribution of income from high-skilled emigrants to lower-income residents, while providing the government with the ability to tax high-income residents. This justifies taxation to reduce the emigration of high-skilled individuals.

4.1.4. Political Perspective

Emigration could also have an impact on the disconnection between a citizen's political rights and obligations. Basically, taxation must always be accompanied by representation. This implies that the compulsory payment must be limited by the laws established by the people's representatives. The taxation with representation jargon, in this case, appears as a condition for political allegiance.

Whereas in the context of emigration, an individual who emigrates does not generally change their citizenship status, i.e. still intends to remain connected with the home country, such an individual commonly maintains their rights as citizens, for instance, obtaining services and protection from embassies, participating in general elections, etc. However, with his relatively long emigration and the possibility of becoming a tax resident in another country, the obligation to pay taxes in the home country no longer exists, but political rights from the home country still exist.[12] Bhagwati (1987, 53) refers to this situation as "no taxation with representation."

This opinion should be a matter of concern by now, specifically with the current pattern of global migration. Conflicts in several regions and the rise of international refugees, demand for talented migrants from population-aging countries, and increasingly loose immigration regulations may lead to the majority of citizens of a country residing in other countries or a country accommodating a substantial number of immigrants. In such an event, the rights and obligations of the population in a country become increasingly asymmetrical.[13] Thus, the tax for emigrants is justifiable.

4.1.5. Efficiency and Revenue Adequacy

Free individual mobility encourages the government of a country to compete for residents and provide optimal budget allocations. Individual choices are assumed to be rational, i.e. choosing a country or jurisdiction considered to be the best in providing public goods. On the other hand, governments in various countries will adjust facilities according to public references (local public goods). In other words, the absence of instruments that limit the mobility of human resources ultimately engenders efficiency.

[12] At the same time, high-skilled emigrants also experience taxation without representation in the host country, where paying taxes generally does not generate any political rights.

[13] The situation can also be reviewed in the fiscal contract model. As the framework of reciprocal relations between the state and the people (the state provides public goods and services and the public pays taxes accordingly) the fiscal contract in the context of an open economy with individual migration has not been addressed by many scholars.

Nevertheless, one question is how a country can finance the provision of quality public goods when facing a brain drain, i.e. the loss of high-skilled individuals, which discourages efforts to boost the economy, as well as revenue mobilization? In the context of sub-national taxes, the measure would be revenue sharing or transfer allocation scheme. However, such a scheme is generally not available in the national or supra-national tax framework.

Hence, the revenue from taxing high-skilled emigrants incentivize developing countries to compete in welfare-improving tax and expenditure. These funds can be used by governments in developing countries to allocate spending to areas that may reduce the motivation to emigrate, e.g. education, industrial parks, safety. However, this argument needs to focus on the connection or link between the revenue from brain-drain tax and its use to prevent emigration.

Further, the poor performance of tax revenue in large developing economies indicates that developing economies require all available options to mobilize revenues and assess tax gaps. Specifically, individual income taxation has not played an important role in the structure of tax revenue, especially when compared to contributions from corporate income tax, VAT/GST, and revenue from extractive industries.

This is mainly influenced by the fact that the majority of individual taxpayers in developing countries have wages below the per capita income or the threshold for allowance. This figure is completely different from the structure of tax revenue in developed countries where individual income tax plays a significant role thus making the tax revenue more sustainable and not susceptible to business or sectoral conditions.

In short, to continuously improve the performance of their tax revenues, developing countries must increase the contribution of individual income tax. Considering that high-skilled emigrants generally have an income exceeding per capita income or the basic exemption threshold, the efforts to tax their income can be justifiable.

4.1.6. Who Provides the Benefits

One of the philosophical grounds for the state to collect taxes is the benefits principle. The next question is what is the role of the home country for skilled emigrants? Questions and criticisms pertaining to this matter have long been discussed. In general, this position departs from the fact that better income and life (and sometimes better tertiary education) are provided by the host country. If such is the case, what is the role of the emigrant country?

The debate must also be supported by the availability of data, but the criticism is not groundless. Allegations that developing countries are

generally not able to provide optimal public goods for the welfare of the society are evidenced by various indicators, in particular, the low government spending on education, health, and infrastructure (Fan, Rao 2003).

However, as suggested by Darvas, Gao, Bawany (2017, 25), it is noteworthy that in general, the level of education of individuals in developing countries is closely related to the economic condition of their families. This implies that the level of income and wealth obtained by families from high-skilled migrants is, in essence, guaranteed by the home country. The guarantee of benefits originates from the protection of property rights, access to financial markets, and political stability. In this context, the home country also contributes positively. From the perspective of the benefit principle, the home and host country are equally justified to impose taxes.

4.1.7. Taxing Rents

According to Bhagwati (1979, 22), another strong argument in taxing skilled emigrants is the fact that the emigrant has windfall gains.

4.1.8. Conclusion

The seven aspects reviewed in the issue of the migration of educated workers to other countries, lead to the conclusion that taxation can be justified. Five of the seven aspects indicate stronger argumentation in favor of taxation, namely the issues of emigration motivation, tax burden and redistribution, political perspective, efficiency and revenue adequacy, and taxing windfall gain. On the other hand, two aspects show the weakness of the argument for taxation, specifically from the benefit theorem and the fact that the emigration of educated workers also gives rise to net gains.

4.2. Tax Policy Options

With (relatively) strong justifications for brain-drain taxation, what policy options are ideal for LDEs? Four policy options, namely the Bhagwati tax proposal, exit tax, tax incentives, and revenue sharing will be reviewed.

4.2.1. The Bhagwati Tax Proposal

The Bhagwati tax proposal refers to the contribution of renowned economist Jagdish Bhagwati, in reviewing the negative effects of brain drain and proposing the main ideas, along with various modifications, fiscal instruments considered ideal for addressing brain drain. This

proposal was made in 1972 and has since evolved, but instead of changing, the basic idea continues to be supplemented, especially in the face of criticisms and information arising in academic debates. Some literature frequently refers to the proposals submitted by Bhagwati as the brain-drain tax because the idea and model are specifically reconstructed to address brain drain.

Bhagwati initially proposed of a tax collected by the host country on immigrants from developing countries. The applicable rate was 15% (surtax) of the emigrant's income. The idea is that the tax collected by the home country's tax authority (in the context of the U.S., IRS) subsequently be transferred to the home country to compensate developing countries for the incurred losses.

This idea was further developed a year later, in cooperation with Dellalfar. With the support of data, they proposed a new rate which is considered more ideal, i.e. 10% for the adjusted taxable income of emigrants from less developed countries. This tax would also be collected for a maximum of 10 years after a person emigrates. The rate-based simulation showed that the potential tax revenue of the developing countries was substantial and far greater than the amount of foreign aid provided by the U.S. in 1971. In the paper, they put forward a more valid argument for brain-drain taxation, which is based on the principle of fairness. Through the fairness jargon, the brain-drain tax aims to compensate developing countries for the lagging and loss of human resources, and if possible, to decrease brain drain.[14] Bhagwati and Dellalfar (1973, 94–96) argue that the tax could be levied by the host country's tax authority or international organizations such as the United Nations. They also proposed to collect the tax with the assistance of the UN and the tax would be distributed to developing countries, with the exception of those that are corrupt and dictatorial.

Until the end of the 1970s, Bhagwati continued to complete his proposal through some scientific work ranging from emphasizing tax administration cooperation through bilateral agreements, underlining the differences between his proposal and revenue sharing schemes, reviewing political aspects, and strengthening the justification of brain-drain tax. Interestingly, Bhagwati (1979, 24–27) also argues that the adoption of the U.S. global tax system that adheres to citizenship-based taxation best enables the implementation of the proposal. In other words, the proposal refers to the U.S. method that deems its citizens as residents regardless of where they are. By using citizenship as a taxation nexus, the connection between the skilled migration and the home country is maintained until

[14] Bhagwati's proposal is criticized as it is considered to add more burden to the emigrants. However, the emigrants are in a better situation as the increase in wages will be greater than the losses.

the change of citizenship status. Thus, a country that recognizes an individual's citizenship maintains its taxation rights.

In fact, almost no countries in the world tax their citizens on their worldwide income. Currently, the U.S. can be considered the only country that has succeeded in enforcing an extraterritorial tax system. Other countries that have attempted the same measure, such as Eritrea (see DSP-Groep BV 2017) and the Philippines (see Pomp 1985), have failed due to weak hegemony and the requirement of support from other countries. This implies that the success of the Bhagwati tax proposal is highly dependent on international cooperation (bilateral or multilateral). In short, taxation of income received by citizens abroad clearly requires assistance and support from the host country, both in terms of collection and exchange of information. Without coordination and exchange of information, the implementation of taxation on foreign-sourced income will be difficult (Keen, Lighthart 2004; Gadzo, Klemencic 2017).

Other criticisms are inseparable from the third-generation research on brain drain in the 1990s. With more accurate migration-related data, many academics have begun to doubt the existence of brain drain and instead showed the gain from high-skilled emigrants. Consequently, there is no moral argument regarding efforts to prevent migration including the absence of justification of brain-drain tax. However, according to Brauner (2010), the Bhagwati tax proposal is substantially driven by fairness, specifically from an economic standpoint and not from an ethical or moral argument. As such, this criticism can be considered not departing from the same perspective.

Although considered to reflect the principle of ability to pay, the Bhagwati tax proposal was also criticized for creating income inequality between skilled and unskilled individuals in the home country. This is caused by the impact of wage improvements for skilled individuals in the country. Consequently, the government's success in addressing unemployment and managing the availability of individual (labor) for certain sectors may be subject to disruptions (McCulloch, Yellen 1975, 249–64).

The Bhagwati tax proposal faces challenges in terms of administration as well. First, it creates compliance costs for individual taxpayers, as well as barriers to working overseas, as mentioned by Desai, Kapur, Mchale (2004, 681). As a matter of fact, developing countries still encounter challenges in taxing individual income. As an illustration, in Indonesia, the contribution from individual income tax other than withholding tax for employees only amounted to less than 1% of the total tax revenue during the 2013–2018 period. Second, the compliance of workers from developing countries working in host countries will be more difficult to ensure as it is far more difficult for them to return to the

home country due to their (financial) ability. This is different from workers from developed countries or at least upper-middle-income countries.

The assessment of the impact on revenue requires an estimation and complete data. In the absence of complete information, the Bhagwati tax proposal may not lead to definite revenues with the double-elimination tax mechanism through exemption and foreign tax credit. Interestingly, a study conducted by Desai, Kapur, and McHale (2004, 683) on the simulation of the application of this tax for India shows that the potential revenue from the Bhagwati tax is substantial. Overall, we have to consider its implications for citizenship changes, especially considering that the only way to be "free" of the tax burden from the home country is the change of citizenship.

4.2.2. Exit Tax

Unlike the Bhagwati tax, the exit tax aims to directly target the core issue of brain drain, which is to prevent losses from the migration of high-skilled individuals to other countries. The exit tax is a tax imposed to create disincentives for the decision of a person or a company to become a resident of another country. According to Larking (2005, 115–62), prior to the change into another country's resident, taxation is imposed on the taxpayer's assets deemed to be disposed of and resulting in a gain. Exit tax is frequently equated to departure tax (immediate exit tax) which is "*... a prepayment of individual income tax levied on resident individuals leaving the country*."

Nonetheless, the exit tax is broader than a departure tax scheme. According to de Broe (2002, 19–78), in addition to being imposed on a person or a company leaving a jurisdiction to become a resident of another country, the exit tax also includes extended tax liabilities as well as recaptures previously enjoyed benefits. However, the extended tax liability is, in reality, more inclined to the application of citizenship-based taxation, which is often discussed together with the Bhagwati tax proposal.

Several countries have implemented the exit tax in their domestic tax provisions. In terms of design, the exit taxes can be divided into two categories, general (all taxpayers' assets are considered) and limited (only a few assets are considered). For instance, Canada imposes a general immediate exit tax which is intended for long-term residents. The tax base is calculated on assets that do not continue to remain in the Canadian tax net and are deemed disposed of before the migration. On the other hand, Chand (2013) specifies that the Netherlands applies a limited exit tax for long-term residents who have substantial shareholdings in companies.

Although considered as one of the instruments to protect the taxation rights of a country as it provides disincentives for emigration, the exit tax is not free of criticism. The main criticism against the exit tax lies mainly in the nature of its imposition, which is applied before an emigrant becomes a resident of another country and earns income there (ex-ante). There can still be options to defer payments from deemed disposal assets. However, considering that an individual who will emigrate from developing economies only has limited income and assets, their decision is barely affected by the presence or absence of the exit tax.

Moreover, the exit tax assumes that emigrants will earn a far better income than what they are paid for from deemed disposal assets. However, the emigrants may or may not obtain good returns in the host country (for instance brain-waste cases). Furthermore, exit tax does not adhere to the principle of ability to pay, as the emigrant has yet to obtain additional economic capabilities.[15] The exit tax is thus considered an inefficient and inequitable policy (Bhagwati, Dellalfar 1973, 94–101).

Challenges also arise from non-economic aspects. The exit tax is considered an instrument that may violate human rights as it prevents a person's mobility to attain a decent living.[16] In the context of the European Union, the exit tax is also frequently debated, in particular, in relation to the Treaty on the Functioning of the European Union (TFEU).

Finally, the administrative feasibility of exit tax collection in developing economies also faces challenges, especially in terms of immigration control and asset appraisal. In developing countries, the obligation to obtain a tax identification number does not apply in general and has no connection to immigration documents. Presumably, this also explains why the exit tax instrument is rarely applied in developing countries.

4.2.3. Tax Incentives

Some countries currently take the opposite measure, i.e. they provide tax incentives, to stop talented and skilled individuals from remaining in a jurisdiction and becoming residents in other countries. This incentive is expected to prevent waves of brain drain. Every country offers varied trial and error programs to obtain an effective design (Agunias, Newland 2012).

For instance, in 2019 Poland plans to abolish taxes for young skilled workers, to prevent them from immigrating to other EU countries.

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[15] The ability to pay is itself one component of the equity principle. See Pistone *et al.* (2019).

[16] See Article 13 (2) of the Universal Declaration of Human Rights: "Everyone has the right to leave any country, including his own, and to return to his country." (*https://www.un.org/en/universal-declaration-human-rights/*)

This income tax revocation incentive is available for residents under the age of 26 who earn less than USD 22,207 (which is above the average wage of Polish residents). One argument for granting this facility is inseparable from the fact that around 1.7 million Polish residents have left the country in the past 15 years.

In the Southeast Asian region, Malaysia has launched the Malaysian Returning Expert Program. The Malaysian Government provides benefits for Malaysian professionals working abroad for at least three years, namely the option of a flat tax rate of 15% on employment income for a period of five consecutive years, tax exemption for all personal effects brought into Malaysia, as well as tax/duties exemption for up to a maximum of MYR 150,000 when purchasing a car.[17] This program is considered quite effective in targeting those who have the option of working abroad (Del Carpio *et al.* 2016). From 2011 to 2018 this incentive was given to approximately 5,024 individuals.

In addition to the incentives provided to citizens, developing countries are also working on a strategy known as reverse brain drain, i.e. the movement of high-skilled individuals from developed countries to developing countries (Gupte, Jadhav 2014, 83–87). As suggested by Cavallini *et al.* (2018, 5), these efforts may encourage competition among countries to attract high-skilled individuals to obtain positive economic and social impacts.

The idea of a tax incentive instrument is frequently discussed as a complementary policy for the implementation of the Bhagwati tax proposal. On a side note, the application of the Bhagwati tax is prone to non-compliance by emigrants abroad. The monitoring, incomplete data, and administrative weaknesses of tax authorities in developing countries are factors that influence such non-compliance, regardless of the penalty feature when the high-skilled migrants return to the home country. Penalties may lead to concerns as they encourage people to remain abroad. To avoid this, Wilson (2008, 2385–91) suggests that tax incentives, for example tax reduction, can in fact be given to compliant taxpayers when they return to the home country.

From the perspective of the tax administration, the provision of tax incentives as a method to address brain drain is clearly more feasible than the other three policy options that require cooperation and/or changes in the international tax system (revenue sharing and Bhagwati tax) as well as reliable assets wealth profiling data (exit tax). The degree of difficulty in applying these incentives is determined by the evidence or documentation by the applicant regarding their eligibility, to the terms

[17] For details on the program visit: ***https://www.talentcorp.com.my/initiatives/returning-expert-programme***

and criteria proposed in the regulations, for example, if the incentives are granted to emigrants with a certain income or who work in certain sectors.

The use of tax incentive instruments is very likely to undermine the equity principle. These incentives may compromise the sense of fairness for citizens domiciled in the country, in particular, high-skilled individuals. A progressive individual income tax will only target educated human resources who generally earn a high income and are "proven" loyal and do not have, or are yet to have, the intention to work abroad. Consequently, this may decrease the trust of loyal high-skilled individuals and encourage their non-compliance or "provoke" them to find ways to obtain the same incentives.

The main criticism against the use of incentives instruments to address brain drain lies in its effectiveness. First, according to Beretta (2017), the competition of providing expatriates with facilities has increased.Today, more and more countries are offering special regimes for expatriates with certain criteria, by mitigating the implementation of their worldwide system, flat tax, etc. Assuming economic rationale, tax incentives provided by developing countries must at least provide a better situation for high-skilled individuals compared to the expected return, plus the additional incentives offered in developed countries.

Second, it seems that the motive for migrating abroad for young workers is not only better income, but also lifestyle and experience, as stated by Heckert (2015) and in the World Youth Report. Thus, the incentives provided to prevent or re-invite emigrants are less efficient, especially for young professionals.

4.2.4. Revenue Sharing

Revenue sharing is one of the policy options proposed by Desai *et al.* (2004), in addition to the exit tax and the Bhagwati tax proposal (global tax system). Bhagwati (1979, 28) states that the scheme may take the form of compensations paid by a developed country to a developing country disadvantaged by the brain drain or brain gains by a developed country from a developing country, notwithstanding the presence or absence of losses in the developing country.

Broadly speaking, revenue sharing schemes can be found in literature on fiscal decentralization, where there is an allocation of revenue from the center to regional governments or between regional governments. Considering that there are currently no international (supranational) organizations responsible for the fiscal area, namely an International Tax Organization, the notion of revenue sharing seems to be more difficult to implement. However, with pressure from the competition for high-skilled individuals and restrictions on migration from developing countries, there

exists a “coercion” to engage in bilateral tax-sharing agreements, as stated by Desai, Kapur, McHale (2004, 684).

5. PROSPECT FOR LARGE DEVELOPING ECONOMIES: SOME COMMENTS

Instead of formulating a final form and practical guidance from various policy options – in particular, for example regarding the implementation of the Bhagwati tax proposal that resembles citizenship taxation – this section explores several points that can help address the prospects of taxes in reducing brain drain in LDE. The points in this section are intended to stimulate further research.

5.1. The Bhagwati Tax Proposal and Non-Discrimination Rule

Bhagwati’s proposal that was developed towards citizenship-based taxation opens the possibility of violations of the non-discrimination principle. In taxation, non-discrimination emphasizes the need for the same tax treatments in the same situations, as well as the justifications for different tax treatments in different situations. In the context of taxation, according to Holmes (2007, 400), the term discrimination is defined as a less favorable tax treatment of a particular tax subject compared to other tax subjects under the same conditions.

In the international tax system, the non-discrimination principle also acts as the most prominent forewarning and is stipulated in Article 24 of the OECD Model, which stipulates the avoidance of discrimination in specific conditions.[18]

With regard to Article 24, it is necessary to distinguish acceptable different treatment (legitimate distinction) and unacceptable treatment (unjustified discrimination). Examples of different acceptable treatment regulated in the tax provisions of many countries are differences in the imposition of taxes that rely on the taxpayer’s ability to pay (ability to pay principle), i.e. as reflected in progressive rates. Different treatments become unacceptable if the objectives are at least based on economic considerations. In short, as argued by Adonnino (1993, 22), such treatment is applied arbitrarily.

The question is: to what extent can differences in citizenship justify different tax treatment?

On further inspection, discrimination in the context of Article 24 of the OECD Model may be defined as: (i) unequal treatment for the same (comparable) cases, or (ii) the same treatment for dissimilar (incomparable)

[18] OECD Commentary on Article 24, Paragraph 2.

cases.[19] In this context, the OECD expressly states that every country that carries out any tax treaty is prohibited from discriminating against the resident status in another contracting state, based on the status of nationality, in applying the tax treaty.[20]

This is stated in Article 24 paragraph (1) of the OECD Model: "Nationals of a Contracting State shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith, which is other or more burdensome than the taxation and connected requirements to which nationals of that other State in the same circumstances, in particular with respect to residence, are or may be subjected. This provision shall, notwithstanding the provisions of Article 1, also apply to persons who are not residents of one or both of the Contracting States."

Through Bhagwati's tax proposal, the use of citizenship-based taxation has the potential to violate the principle of non-discrimination. As the scheme provides different (dissimilar) tax treatment under the same conditions, namely where non-resident citizens and non-residents are treated differently, i.e. one home country has the taxing rights while the other does not.

5.2. Exit Tax Is Only Appropriate for Emigration Driven by Tax Motives

The experiences of various countries related to exit taxes provide an important lesson, i.e. even though the exit tax prevents the transfer of resident status for individuals, its application serves as an anti-avoidance provision (Kubicova 2016). Put differently, it acts as an instrument to prevent changes in resident status triggered by tax motives, either in the context of avoiding capital gains tax or an effort to seek lower tax burdens in other jurisdictions.

Such a statement can be proven by the implementation of the exit tax provision as one of the six measures initiated by the European Union in the Anti-Tax Avoidance Directive (ATAD). Unfortunately, none of the ten LDEs reviewed as case studies in this article apply an exit tax. However, lessons from similar developing countries, such as South Africa, have shown that the exit tax is intended to prevent emigration encouraged by tax motivation (Mazansky 2010).

From the perspective of large developing economies, the application of an exit tax would be more relevant if associated with high-net-worth individuals. This proposal is further driven by the notion that with the

[19] According to IBFD (2005, 124), discrimination is defined as "In international tax context discriminations most often takes of the form of different treatment of taxpayers whose situations are comparable except in respect of characteristics such as nationality."

[20] Nationality is defined as citizenship status for individuals or, for companies,the place where it is established.

non-optimal tax system and governance, changes in HNWI's resident status in developing countries may be motivated not only by tax factors but also related to efforts to cover up illicit financial flow, corruption in the political sector, and transnational crime (Buchanan, McLaughiln 2017, 8–9).

5.3. Bhagwati's Tax Proposal Without Earmarked Budget is Ineffective

The issue of brain drain alone cannot be completely resolved with citizenship-based taxation rights, embodied in the Bhagwati tax proposal. Citizenship tax can only address the prevention of potential revenue forgone from the tax base (citizens) that emigrate, but it is not necessarily effective in preventing emigration (loss of human resources). In essence, citizenship tax does not create a disincentive for high-skilled individual to emigrate, since the decision to emigrate may not be compelled by the tax factor in the home country as a push factor, implying that they can enjoy a high income in the host country while still contributing to the home country through taxes

Moreover, considering that brain drain is a loss for the home country, due to the loss of skilled human resources beneficial to economic development, revenue from citizens who become residents of other countries can only reduce the impact of brain drain if it is directly dedicated to improving the labor market, education, and R&D in the home country. Without an earmarked budget scheme, home countries can find themselves in a situation that resembles the "flypaper effect" (Crowley, Hoffer 2018). In the absence of an earmarked budget, the Bhagwati tax proposal cannot restore the pre-conditions of brain drain, but only serves as a "tool" to increase individual tax income revenue at the global level.

In non-benevolent or corrupt and authoritarian governments, revenue without an earmarked budget can also encourage inappropriate behavior. In reality, this discourages the government to invest in the provision of quality public goods, while concurrently "transfering" the government's responsibility to another country and encouraging emigration to transfer the "burden" of public goods provision, by allowing a maximum flow of emigration, thus (prospective) high-skilled citizens may (attend school and) earn income. In return, the government obtains tax revenue from the emigrants.

5.4. Prospects of Global Acceptability of the Bhagwati Tax Proposal

There are at least three things to consider regarding the prospects of implementing the Bhagwati tax. First, with the increasingly relevant concept of citizenship-based taxation, there will be potential for asymmetrical taxation rights in the future. Disputes and debates on

international tax fora related to personal and economic connecting factors may re-emerge.[21]

The fiscal preferences and tax sovereignty of each country seems to be too strong to simply "succumb" in order to address the brain drain issue. As such, middle-ground solutions are required, for instance, the abandonment of the principles of residence and citizenship, which would be replaced by time-tests that better reflect increased individual mobility (Beretta 2019, 107–10).

Second, there is a concern that with the transition to citizenship-based taxation, each country will compete to discourage the change of citizenship status (for home countries) or offer the change of citizenship status (for the host country).[22] The former presumption is most likely true, while the latter is not necessarily the case. The migration policy and citizenship status of a country will be increasingly relevant in regard to a culture of openness and will be influenced by national security issues (Adamson 2006, 165–99). Thus, any matter that may "disrupt" the national security agenda is subject to long and careful consideration.

Third, the prospect of successful implementation of the Bhagwati tax will depend on how the proposal is linked to the world's main concerns. Accordingly, the brain drain issue and the Bhagwati tax proposal must be linked to a new development agenda (Brauner 2010), in which case, large developing economies, along with BRICS countries (Brazil, Russia, India, China, and South Africa), may play an important role in advocacy at the global level (Pistone, Brauner 2015, 385–92).

5.5. Citizenship-based Taxation Tests the Consistency of Developing Countries Concerning Favor Towards the Source Country

The Bhagwati tax proposal is heading towards taxation in favor of the citizen's country (highlighting personal attachment) whereas to date,

[21] This primarily relates to dual residents. Article 4 paragraph (1) of the OECD and UN Model does not define resident taxpayers. Provisions concerning such a matter are stipulated in the domestic provisions of the two countries establishing the tax treaty. As such, what determines whether a tax subject is a resident taxpayer in the countries that enters into the treaties is based on the domestic provisions of the two countries. If the tax subject is a resident taxpayer in both countries (dual resident), Article 4 paragraph (2) and (3) provide guidance to address the dual resident issue through a tie-breaker rule that aims to prevent double taxation, hence the tax subject may only be a resident taxpayer in one country. Subsequently, the tie-breaker rule determines the residency status of an individual through the tests of a permanent home, vital interest, habitual abode, nationality, and through Mutual Agreement Procedure (MAP). See Schwarzenhofer (2005, 20) for further reference.

[22] Presently, many countries have offered citizenship by investment, as practiced by Cyprus, Malta, Moldova in Europe, and Dominica, Grenada and St. Lucia in the Caribbean.

most of the capital importing countries – which are developing countries – tend to be proponents of the source country (highlighting economic attachment). On various occasions, developing countries often voice their demands for a fairer (greater) allocation of taxation rights to the source country as well as "accusations" against the OECD Model (Pistone, Brauner 2015, 480). The siding results from the differences between the OECD Model and the UN Model – as a representation of developing countries.

The demand of developing countries, as importers of capital, for greater taxing rights for the source country stands on the argument that active economic activities are, in essence, carried out in the source country (sometimes referred to as the market jurisdiction). Conversely, the taxing rights of the resident country, as the location of the capital owners, should be limited.

In the context of the Bhagwati tax, the position of developing countries (labor exporters) may differ. Are the arguments for granting taxation rights to developing countries also valid and in favor of the same principles when developed countries (capital exporters) claim their rights? This question is worth exploring and can lead us to other intense discussions, such as whether the host country (a developed country) will demand a withholding tax mechanism or not.

5.6. Revenue Sharing and Demand for an International Tax Organization

Revenue sharing is essentially made possible through the presence of global organizations in the tax sector. In 2015, at the UN Third International Conference on Financing for Development, held in Addis Ababa, Ethiopia, there was a discussion and plan to establish an International Tax Organization (ITO).[23] G77 developing countries were initially eager to permanently transform the UN Committee of Experts on International Cooperation in Tax Matters (UN Tax Committee) into the ITO, as a global tax system formulation mechanism that no longer requires that the OECD play a role. This idea was challenged by developed countries. In the end, the forum only agreed to strengthen the UN Tax Committee's capacity, and not to its transformation.

In some literature, the ITO is expected to perform several functions, for instance, monitoring trends and statistics concerning the tax situation on a regular basis, acting as an international tax forum, providing advice and solutions to global tax problems, and supervising information exchange cooperation (Tanzi 2016). Although interesting, the notion of

[23] In this conference, 193 countries agreed to improve the performance of state revenue mobilization. These efforts are called for to finance 17 Sustainable Development Goals (SDG's) 2016–2030 agenda, as a further commitment of MDG's.

the ITO conflicts with tax sovereignty. The tax sovereignty is intended to maximize the welfare of the population, guarantee income redistribution, oriented towards national interests, side with the community, and guarantee democratic values (Dagan 2013).

Clearly, ITO would reduce the freedom of each country to design its tax system in accordance with its national orientation. Such an opinion is not fully acceptable. As a matter of fact, the ITO is believed to be able to guarantee tax sovereignty (Dietsch 2015). After all, the tax sovereignty of every country has been eroded without the ITO. The sovereignty of countries in designing corporate income tax policies has diminished. As pointed by IMF (2014, 13), governments are now unable to formulate tax policies in a "closed" environment, but consider the measures currently undertaken by other countries and how they may impact the economy. The ITO guarantees tax sovereignty to the same degree in all countries.

The idea of the ITO is increasingly relevant to the fact that tax non-compliance and fair allocation of taxation, caused by increased labor and capital mobility amid various tax systems of different countries, has become a global issue. Securing the tax base from erosion can now be categorized as one of the global public goods, not unlike environmental sustainability, the stability of international financial markets, global security, and others (Kaul *et al.* 2016). The ITO is an expected solution to the tragedy of commons, which in this case refers to fair share tax (Tanzi 2016, 256–59).

5.7. The Relevance of Substantive and Enforcement Jurisdiction

When Bhagwati submitted his proposal more than 40 years ago, the idea of supporting tax collection by the host country seemed utopian. In the course of time, the discussions regarding the development of international taxation, specifically in the context of the digital economy, underline the increasing relevance that the role of jurisdictions in collecting taxes that they are not entitled to.

Hellerstein (2003) proposes a new concept in terms of tax jurisdiction, with two jurisdiction categories, based on their power to tax, namely the substantive jurisdiction, related to the power of a state to impose a tax on the subject matter of an exaction; and the enforcement jurisdiction, related to the power of a state to compel collection of the tax over which it has substantive tax jurisdiction.[24]

[24] As quoted by Hellerstein (2003): "*Substantive jurisdiction to tax includes such questions as whether a state has the power to impose a tax on the income that a non-resident earns from sources within the state, or to impose a tax on goods or services purchased outside but consumed within a state. ... Enforcement jurisdiction includes such questions as whether a state has power to enforce the collection of a tax on income earned by a non-resident from sources within the state, or whether a state has power to enforce*

This classification can be applied both in terms of income tax and consumption/value added tax and has four possible scenarios, namely (i) the substantive and enforcement jurisdictions are both available; (ii) the substantive jurisdiction is available but the enforcement jurisdiction is not; (iii) the substantive jurisdiction is not available, but the enforcement jurisdiction is; (iv) neither the substantive nor the enforcement jurisdiction is available. Problems arise if the combination does not occur symmetrically (both are available/not available).

In other words, the policy design of substantive and enforcement jurisdiction allocation should be one of the points to be formulated, especially in the context of the Bhagwati tax proposal. Furthermore, we should be aware that the principle of sovereignty prevents a country from claiming taxes in areas outside the country without strong taxation rights. Fortunately, at the international level, assistance in tax collection has been made possible by the 2003 revision of the OECD Model.[25]

5.8. Promoting Tax Incentives as a Quick Response

Within the framework of tax competition, the tax incentive instrument is the best and most rational way for developing countries to help ensure their involvement in the global arena. Compared to Bhagwati's proposal, tax incentives are a relatively risk-free domestic instrument as opposed to the international tax system (for example, treaty override potentials).

Moreover, concerns about the massive development of tax incentives, which may lead to harmful tax practices frequently mentioned in the Base Erosion and Profit Shifting (BEPS) Project Action Plan 5, are groundless. Tax incentives related to the migration of residents are connected to substantial economic activity (OECD 2019). Notably, in the context of brain drain, the generally debated income is the salaries of employees that are part of active economic activities.

As such, to what extent can tax incentives be effective in addressing the issue of brain drain? The answer is unclear, given that in the context of brain drain, the motive is not always the tax factor in the home country. Nonetheless, efforts to design incentives that can exceed quantified returns and non-economic factors (lifestyle, ease of bureaucracy, etc.) are worth trying. To be more effective, as suggested by Del Caprio *et al.* (2016), it would be best if the tax incentives were embodied and combined with other non-tax incentives.

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the collection of a tax on goods or services purchased by an in-state consumer from a remote vendor."

[25] See Article 27 and Commentary of the OECD Model Tax Convention regarding Assistance in the Collection of Taxes.

Tax incentives can also be designed to create an ecosystem that keeps high-skilled individuals in the home country, for example, cost-based tax incentives (e.g. for R&D activities, training costs for certain skills) or profit-based incentives (tax holiday for labor-intensive sectors). These incentives would encourage technological development, improve the quality of human resources, and ensure employment for certain skills.

6. CONCLUSION

Considering the situation in large developing economies regarding international migration, the use of tax instruments in addressing the brain drain, although weak, is justifiable, especially considering the fact that they also enjoy benefits from high-skilled emigration, ranging from high remittance rates, reduced unemployment, prevention of social unrest, and a large tertiary-educated population in their countries. There are at least five things that can be concluded from the assessment of the four policy choices.

First, there is no stand-alone tax policy that can optimally address brain drain, in the sense of reducing the number of high-skilled individuals who emigrate. An exit tax may serve as the best possible policy, however, considering that the majority of individuals from large developing economies do not yet have sufficient wealth and income, the imposition of an exit tax shortly before departure abroad will not have much effect. Moreover, the exit tax is more appropriate if associated with the issue of preventing tax noncompliance, such as tax avoidance and tax evasion.

Second, most policies focus more on the element of fairness to compensate for the "loss" caused by the host country. This is found in Bhagwati's tax proposal and revenue sharing, which prioritizes a "guarantee" of revenue for the home country. For large developing economies, this guarantee of revenue is certainly useful, but without an earmarked budget scheme to improve the economic situation and job opportunity, such a guarantee may encourage misallocation, and therefore the root causes of brain drain would remain.

Third, almost every available policy requires better coordination at the international level. Potential non-discrimination principle and dual resident violations (the Bhagwati tax proposal) and dependence on the existence of international tax organizations (revenue sharing) undermine human rights since they discourage migration (exit tax). In this context, tax incentives seem to be the most rational policy. One thing is certain, the role and voice of large developing economies are called for (though they may not necessarily be influential) in order to raise the issue of resolving brain drain in international forums.

Fourth, all policy options require closer collaboration with immigration agencies. All taxable events, as well as the enforcement of

these policies, require clearer information on the immigrants' home country, duration, time of return, migrants' economic capacity, and background. At the present, the capacity of the tax administration, especially the cooperation in information access among tax authorities and immigration authorities in developing countries may be suboptimal.

Fifth, each policy has the potential to produce unintended consequences. For instance, there is competition for nationality status and a wave of tax incentive competitions for highly– talented individuals. These two things will ultimately be unable to constrain migration rates.

In conclusion, notwithstanding the fact that the available options are quite promising, there is no ideal policy. In the end, the problems raised in this paper are expected to stimulate future research.

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Giorgio Beretta, PhD[*]

'FIXING' THE SOCIAL CONTRACT: A BLUEPRINT FOR INDIVIDUAL TAX REFORM[**]

In the face of population ageing and demographic decline, nowadays all countries compete for an increasingly valuable asset: human capital. Indeed, the drain of human capital from one country to another concerns not only highly-skilled individuals seeking job opportunities abroad, but also pensioners relocating to sunnier and more tax-friendly jurisdictions. Absent global action, the risk of uncoordinated and unilateral measures taken by countries to increase and protect their own tax base, with adverse effects both from the inter-nation and the intra-nation equity perspective, is very concrete. So far, however, neither the OECD nor the European Union have developed specific policies or measures in the domain of individual taxation. Arguing that scope of reform exists also in this field, the article explores various policies and measures as a blueprint for individual taxation reform, with the double aim to curb tax competition among countries and fix the crumbling social contract.

Key words: *Human capital. – Individual taxation. – Migration. – Social contract. – Tax policy.*

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'*Society is indeed a contract ... As the ends of such a partnership cannot be obtained in many generations, it becomes a partnership not only between those who are living, but between those who are living, those who are dead, and those who are to be born.*'

(Burke 1790)

'*It is no longer the call to 'Give me your tired, your poor, your huddled masses'; now we ask for your alert, your privileged, your brainy, your talented. Our machines can do the menial work. Today the emphasis is on technical skill, sophisticated training and adaptability to modern society.*'

(Perkins 1966, 617)

'*A place in the sun and a tax-free pension*'

(Somerset Webb 2015)

1. INTRODUCTION

The launch and subsequent delivery of the broad and multifaceted Base Erosion and Profit Sharing (BEPS) 15 Action Points in 2013–2015 undoubtedly marked a turning point for international taxation (on BEPS, see Christians, Shay 2017; Brauner 2014). After BEPS, in fact, no one can seriously hold the traditional view of a completely sovereign autonomy of countries in tax matters (for a discussion, see Rocha, Christians 2017). As a matter of fact, major theoretical developments in tax policies are now achieved not only through political and legal processes undertaken at the national level, but also in a multilateral setting and with the increased participation of non-governmental actors.[1] In the past the OECD has been and, certainly still is, the major organization to act as a central hub for shaping international tax policies (see, especially, Cockfield 2005).

The action spearheaded by the OECD and undertaken by all countries participating to the Inclusive Framework on BEPS,[2] however, has narrowly focused on closing tax loopholes exploited by multinational

[1] An example of the increasing intervention of non-governmental actors in a global tax governance is given by the Platform for Collaboration on Tax, launched in April 2016 by the International Monetary Fund (IMF), the Organisation for Economic Co-operation and Development (OECD), the United Nations (UN), and the World Bank Group (WBG).

[2] The OECD/G20 Inclusive Framework on BEPS was established in 2016 as a means to ensure interested countries and jurisdictions, including developing economies, can participate on an equal footing in the development of standards on BEPS-related issues, while reviewing and monitoring the implementation of the OECD/G20 BEPS

enterprises (MNEs) and has sought to establish a new international tax order in the field of corporate taxation only (see, especially, Christians 2016).[3] Remarkably, no action has so far been taken at the international level in the realm of individual taxation. The same has indeed occurred in the European Union (EU), where the fight against Harmful Tax Competition (HTC), since the establishment of the Code of Conduct Group in 1997, has only revolved around the identification and elimination of preferential tax regimes designed for companies and other legal entities.[4]

Such dearth of action is rather surprising given that, although revenue losses for national governments due to international tax evasion and avoidance are far greater in the corporate sector, the number and extent of threats arising in the field of individual taxation are by no means negligible.[5]

The author indeed posits that three distinct challenges – each of which is somehow referred to in the three passages quoted in the epigraph – deserve, in particular, closer attention. The first challenge is related to the threat posed to the social contract by the combined effects of population ageing and demographic decline in nearly all developed countries, which contribute to a widening divide across generations and urge governments all around the world to search for additional sources of revenue. The second challenge is related to the phenomenon of the brain drain, which sees countries fiercely competing among themselves for increasingly valuable assets such as human capital and poaching one another's pool of talented individuals. The third challenge is related to the increasingly large wave of pensioners who migrate from one country to another in search of a milder climate and often a more tax-friendly environment, which causes a revenue drain in the country where pension income was built up and/or from which it is paid out.

Project. As to October 2019, over 130 countries and jurisdictions are collaborating on the implementation of the BEPS 15 Action Points.

[3] Notably, in pursuit of the BEPS goals, countries have committed to implementing four minimum standards, respectively concerning measures on Harmful Tax Practices (HTPs) (Action 5), on Tax Treaty Abuse (Action 6), on Country-by-Country (CbC) Reporting (Action 13), and on a Mutual Agreement Procedure (MAP) (Action 14), all of which, however, relate only to corporate taxation (see OECD/G20, 2019a).

[4] This in spite of the fact that the Preamble of the Resolution on a Code of Conduct, of 1 December 1997, explicitly contemplated the possibility to tackle HTC practices also with regard to 'special tax arrangements for employees' (see European Commission 1998, 1). A similar plea was then reiterated by the Commission in its 2012 Communication titled 'An Action Plan to Strengthen the Fight against Tax Fraud and Tax Evasion', but it did not actually lead to the enactment of any measure in this field (see European Commission 2012a, 7).

[5] Notably, revenue losses for governments due to BEPS practices by MNEs are conservatively estimated by the OECD at around 4–10% of global corporate income tax revenues or USD 100–240 billion annually (see OECD 2019a).

While all these three challenges indeed point to the need to undertake global action in the field of individual taxation, with a discussion of each of them provided in the following, in terms of proposals, the article mostly focuses on migration of pensioners and cross-border taxation of pension income. Despite such a narrow context, the author submits that the proposed policies and measures may offer valuable suggestions for rethinking individual taxation on a more general scale.

The article is organized as follows. Section 2 provides background information on the increasing challenges faced by the implicit social contract, which underpins the Welfare State currently adopted by nearly all developed countries. In particular, the discussion centres around the threats posed by a widening divide across different generations. Section 3 traces the main causes and consequences of the brain drain and the battle for human capital which is fiercely being waged by countries worldwide. Section 4 describes the phenomenon of migrating pensioners as well as the main features of the different pension taxation regimes. Section 5 deals with taxation of pension income on an international plane, with focus on the treatment currently provided under the OECD Model. Exploration of the tax treatment of pension income at the international level is used for individualizing possible policies and measures to be enacted in the field of individual taxation. This task is undertaken in Section 6, where a blueprint for individual tax reform is laid down, and pros and cons of each proposed measure are closely compared. Section 7 concludes.

2. THE SOCIAL CONTRACT UNDER THREAT AND THE WIDENING INTERGENERATIONAL DIVIDE

We are arguably entering an age of increasing global instability and social disillusion, both of which may be seen as prominent hallmarks of the end of the globalization thrust and the beginning of an opposite ‘deglobalization’ era (see, especially, van Bergeijk 2019; James 2017). The symptoms of a growing instability and disillusion are variably expressed in politics, society and the economy, in so far as all these areas are experiencing a surge of nationalist and protectionist movements, fuelled by popular grievance and general distrust of elites (see, in this regard, Lagarde 2019). In the aftermath of the financial crisis of 2008, it has in fact become common for people, especially the middle-class in developed countries, to have declining perceptions of well-being and trust in the future,[6] whereas the global wealthiest one percent has gained

[6] According to OECD (2019b, 13), due to nearly stagnating wages, growing lifestyle costs and housing prices, rising job insecurity in the middle of fast-transforming labour markets, ‘today the middle class looks increasingly like a boat in rocky waters’.

enormously throughout the past decades (for different perspectives in this regard, see Smith *et al.* 2019; Piketty 2013).

Rising inequality – both at the national and international level – is certainly a major source of government and individual concerns (see, for example, Wilkinson, Pickett 2019; Stiglitz 2015), as indeed those worries are further exacerbated by gloomy forecasts of employment conditions in the near future due to the rapid pace at which epochal phenomena such as automation (see, for a discussion, Baldwin 2019; Ford 2015) and population ageing[7] are occurring.

The Welfare State, adopted after World War II by nearly all developed countries, since it is seen as a valuable weapon against inequalities in society, is currently under tight scrutiny.[8] This is largely due to the social contract implicitly agreed upon between generations, which underpins the Welfare State and, arguably, contributes to holding a society together (for a perspective on the situation in this regard in the United Kingdom, see House of Commons 2016, 8–23).

The intuitive idea of such an intergenerational social contract is that the redistributive mechanism underpinning the Welfare State justifies the obligation of the current productive generations to finance the health, pension and care services of the older generations, by arguing that future generations will provide the same kinds of benefits once the current generations retire (see Hammer, Istenič, Vargha 2018, 22). In this way, the Welfare State facilitates solidarity across different generations or age cohorts, via financial transfers to the old, mainly in the form of pensions, and to the young, mainly in the form of education, both of which are funded principally by taxing the current working-age population (see Resolution Foundation 2018, 25–27).

But there is a catch. In principle, everyone is to pay in during their working life, drawing down in early years and retirement, for a broadly neutral lifetime result. However, the amount of transfers and benefits provided in return may well change over time, as indeed do tax rates and the size of generations that are contributing or withdrawing. As a result, over their lifetime span, different generations can end up with net gains or net losses, a circumstance that is very much capable of skewing the redistributive mechanism underpinning the Welfare State (see Gardiner 2016, 7).

[7] Tellingly, by 2020, for the first time in history, there will be more people on the planet over the age of 65 than under five (see He, Goodkind, Kowal 2016, 3).

[8] As early as 2000, Avi-Yonah (2000, 1578) warned that ‘globalization leads to a more pressing need for revenues at the same time that it limits governments’ ability to collect those revenues. This dilemma threatens to undercut the social consensus about the value of the Welfare State that underlies modern industrialized societies and to create a backlash against the globalization that produces too many overall benefits’.

Presently, there is in fact a widespread consensus that the social contract is not being honoured for today's younger generations and that, in particular, the Baby Boom generation, commonly identified as individuals born between 1945 and 1965, are receiving a net gain over later coming generations, such as those of the Generation X, i.e. individuals born between 1965 and 1980, and the Millennials, composed of those born between 1980 and 2000.[9]

Worries on this matter concentrate, in particular, on this latter age cohort. Tellingly, the Resolution Foundation (see Gardiner 2016, 5) has revealed gloomy economic forecasts for those belonging to that generation, signalling that Millennials are 'the first generation that has so far earned less than the one before at every age' and warning that, if productivity growth remains as low as now, 'Millennials are at risk of becoming the first ever generation to record lower lifetime earnings than their predecessors'.[10] On a similar strain, European Commission (2017, 12) has flagged increased concerns that today's young people in the EU and their children may actually end up worse off than their parents. Concerns also surround the future pensions of current workers, whose social sustainability is indeed put under a severe test, in so far as it is not clear whether the amount of the present contributions will provide adequate living conditions for tomorrow's retirees (see, especially, Scarpetta, Blundell-Wignall 2015). On a broader perspective, there is also a risk that a growing intergenerational divide would widen inequalities and wealth gaps existing in society, therefore the overall importance of inheritances and private transfers between generations is expected to grow (see Resolution Foundation 2018, 114–117).[11]

Such dire prospects for today's younger generations are indeed the ultimate fruit of various ongoing trends in society and the economy. The

[9] This classification of generations follows Willetts 2010. One should caution, however, that defining different generations inevitably entails an element of arbitrary choice, as long as, for instance, those individuals born immediately before a generational dividing line may well dispute their implicit association with those born20 years earlier, for example, but not with those born only one year later.

[10] Such gloomy prospects, however, are contested by others (see, for example, Ganesch 2016), who point out, for instance, that economists indeed 'cannot account for the dazzling consumer gains that come with technology and competition multiplied by the passage of time', perhaps embodied at best by 'all the facilities now inherent to a smartphone' which 'would have cost a teenager in 1980 a king's ransom in separate, clunky machines'.

[11] See also Bangham (2018, 3–6), pleading for the elimination of the UK current inheritance tax and its replacement with a lifetime receipts tax to be levied on recipients with fewer exemptions, a lower tax-free allowance and lower tax rates, whose revenues are to support a GBP 10,000 'citizen's inheritance' – a restricted-use asset endowment for all young adults, from the age of 25, to sustain skills, entrepreneurship, housing and pension savings.

first challenge is related to population ageing, due to a combination of an increased life expectancy and a decreasing trend in birth rates in nearly all developed countries,[12] both phenomena that indeed are expected to intensify in the coming decades, so that a growing demand for health, pension and care services will have to be sustained by the fiscal revenues extracted by a shrinking working-age population, thus increasing the so-called 'dependency ratio', measuring the number of pensioners per working age person (see Resolution Foundation 2018, 87–89).[13] Next, it comes the inequality challenge, with an increasing share of wealth globally owned by older generations, who have managed to shield their income and assets from the financial crisis of 2008 better than the younger generations (see Gardiner 2016, 23–25). The third challenge is related to poor job prospects for the young, who, mainly due to fast-paced automation, experiences increasing challenges in finding an employment, at a time when overall job quality, particularly in terms of work stability and benefits provided, has been reduced dramatically (see, especially, OECD 2019c).

As a result, a new divide is ripping society apart and it is based on age, in so far as when a person was born increasingly matters in determining their present and future living standards.[14] This situation, of course, generates significant backlashes – often depicted even in terms of 'intergenerational warfare' (see, most notably, Willetts 2019; Pickard 2019) – across generations and in society, further fuelled by a misleading propaganda on both sides (see, especially, Sternberg 2019; Bristow 2019). Older generations are thus depicted as a gerontocracy of the early-retiring and asset-rich, in contrast to precariously housed and insecurely employed younger generations,[15] whereas the latter are accused of living frivolously and have even been caricatured for consuming avocado toast (!) and

[12] Indeed, as revealed by He, Goodkind, Kowal (2016, 15), birth rates in all countries, with the exception of African ones, are already below the so-called 'population replacement level', which is the number of children per woman needed to sustain population replacement.

[13] Against this backdrop, it may be contended (see, for example, European Commission 2018a) that an ageing population eventually favours private expenditure on a whole new set of goods and services, from connected health devices to age-friendly universities, all of which contributing to the flourishing of the so-called 'silver economy'.

[14] Evidence of such growing divide between the old and the young became apparent with the Brexit referendum, which indeed showed that British politics is deeply polarized by age, with a substantial majority of older people voting for leaving the EU, while a large majority of younger generations voting for remaining in the Union (see Norris 2018). It should also be noted that, as their own population grows older, the political weight in all developed countries becomes increasingly tipped in favour of older generations.

[15] For instance, the New York Times columnist Thomas Friedman (Friedman 2010) has gloriously railed against 'a Grasshopper Generation', one that 'has eaten through all that abundance like hungry locusts', whereas David Willetts (Willetts 2010),

priced coffee, instead of working and saving for the future as, supposedly, former generations did (see Levin 2017).

3. BRAIN DRAIN, TALENT AND THE INTERNATIONAL BATTLE FOR HUMAN CAPITAL

New kinds of wars are being waged by many countries all around the world for hoarding an increasingly valuable asset: human capital.[16] Human capital can broadly be described as all the wealth of knowledge, skills, competences and attributes – which, overall, might be labelled as 'super talent'[17] – that a few of individuals are endowed with and that facilitate the creation of personal, social and economic prosperity, being all of these preconditions for the flourishing of the 21st century 'knowledge society' (for a conceptualization, see Drucker 1993). As a proxy for all these endowments, educational attainments of those individuals are generally used.[18]

Amid those international wars and battles (see, in this regard, Brücker *et al.* 2012), countries' victories and losses against one another are measured by means of inbound and outbound flows, i.e. by looking at the overall number and quality of the endowments of individuals permanently moving in or out the territory of the given country. Indeed, this two-way flow is neither necessarily nor under all circumstances well-balanced. Quite the contrary, such flow can be one-way. If this 'human capital' exchange is overall positive, i.e. more highly-skilled individuals are moving in rather than out, the country has a 'profit' or, more appropriately, a 'brain gain'. On the other hand, if for a given country the

chair of the UK Resolution Foundation, has claimed that 'the Baby Boomers took their children's future'.

[16] Although the origins of the expression can be traced as back as to Adam Smith (1723–1790), the modern usage of the term 'human capital' is generally attributed to Gary S. Becker (1930–2014), especially in regard to his influential book *Human Capital: A Theoretical and Empirical Analysis, with Special Reference to Education*, first published in 1964.

[17] According to Shachar, Hirschl (2013, 72), '[t]he desire to be great, to make a lasting mark, is as old as civilization itself. Today, it is no longer measured exclusively by the size of a nation's armed forces, the height of its pyramids, the luxury of its palaces, or even the wealth of its natural resources. Governments in high-income countries and emerging economies alike have come to subscribe to the view that something else is required in order to secure a position in the pantheon of excellence: it is the ability to draw human capital, to become an "IQ magnet", that counts'.

[18] In this connection, however, it should be noted that the category that is used to qualify an individual as highly-skilled is related to the possession of tertiary education, an element that by itself is very crude, in so far as it includes in this category even individuals with (only) practical and technical education degrees. For an overview about education classification at the international level, see UNESCO 2012.

said balance is overall negative, i.e. more highly-skilled individuals are moving out rather than in, it faces a 'loss' or, more appropriately, a 'brain drain' (see Boeri 2012, 1).

The expression 'brain drain' was first coined by the British Royal Society (see Royal Society 1963) to narrowly describe the outflow of scientists and technologists from the United Kingdom to both the United States and Canada in the 1950s and early 1960s.[19] However, presently, the term is more broadly used to illustrate the departure of highly-skilled individuals – thus, not necessarily scientists or technologists – from their own countries to others where usually wages and life conditions are more favourable overall, or are at least perceived as such.[20] As a break-down of this compound expression suggests, the word 'brain' refers to the wealth of knowledge, skills, competences and attributes with which the emigrating individuals are believed to be endowed. The word 'drain' implies that the rate of those leaving a country is far greater than the normal or desirable level of departures from a country. The link between these two words means that the departure of the most talented and highly-skilled individuals from a country actually occurs at an appreciable rate (see Giannoccolo 2009, 2).

Brain drain is indeed the source of major concerns for governments and policy makers in the countries of origin (see, for example, *The Italian Insider* 2019; Filipovic 2019), which especially complain about efficiency losses to their economy or, even, about the shortage of talented people in specific economic sectors (e.g. in the healthcare or education sector), in so far as those nations blame the country of arrival for poaching their own base of talented individuals, whose education and training were often financed by means of fiscal revenues, so that an export of its 'human capital' effectively becomes a sunk investment for the country of origin.[21]

[19] If the emigrant is an unskilled individual, then one could perhaps speak about 'muscle drain' rather than 'brain drain' (see Pomp 1985, 250, 260 and 286).

[20] Compare the definition of 'brain drain' contained in the Cambridge English Dictionary ('the situation in which large numbers of educated and very skilled people leave their own country to live and work in another one where pay and conditions are better') with the narrower one included in the Collins English Dictionary ('the movement of a large number of scientists or academics away from their own country to other countries where the conditions and salaries are better'). For their own account, EU institutions (European Commission 2019) define 'brain drain' as 'the loss suffered by a country as a result of the emigration of a (highly) qualified person'.

[21] Tellingly, a 2019 report prepared by the Westminster Foundation for Democracy (2019, 23) for the UK government estimates that the 'sunk' cost of education of emigrants from a country such as Serbia in a single year is more than the total annual earnings from the IT services exported by that country. On the other hand, it could be contended (see Boeri 2012, 9) that 'selective immigration policies increase individual incentives to invest in human capital in the sending countries, so that the impact of migration on human capital formation in the country of origin may not be so strong'.

Although the general thrust of the conventional view is that the emigration of human capital is detrimental to a country, the actual validity of such a statement is open to discussion, as it is related to an empirical question whose answer varies from case to case (see, especially, Kapur, McHale 2005; Commander, Kangasniemi, Winters 2004). Moreover, literature also points out that, to the extent that the brain drain allocates human capital resources more efficiently, such phenomenon is likely to benefit more people globally (see Sykes 1992, 1). From another perspective, it is also contended that the brain drain is nothing more than the free exchange occurring across country borders, in as much as goods and services flow in and out a country (see, in this regard, Carens 1987),[22] which states professing a liberal creed certainly cannot obstruct, at least if they have committed to respect fundamental human rights such as freedom of movement, which is even enshrined in several international charters and declarations.[23] Lastly, there are additional phenomena related to brain drain, such as remittance, diasporas and returns, whose net effects on the country of origin are difficult to assess (for a discussion, see Faini 2017; Wei, Balasubramanyam, 2006; Dustmann, Fadlon, Weiss, 2011).

Various reasons can be traced at the roots of the brain drain phenomenon. The main determinant of the brain drain is generally recognized as being the wage differentials existing between countries, which may function as either a push or pull factor for both inbound and outbound migration patterns (see, especially, Borjas 2001). Another traditional factor encouraging migration is related to cross-country unemployment differentials (see, especially, Piracha, Vadean 2009). The quality of public institutions and standards of living may also help explain the decision of an individual to migrate from one country to another (see, especially, Cooray, Schneider 2016). Other non-financial benefits could equally motivate talented and highly-skilled individuals to move from a country, such as the existence of centres of excellence in a specific economic sector in the country of arrival: in a sense, 'brains' go where other 'brains' are (see Tesón 2008, 902).[24] Intended as such, the brain drain – like any other economic phenomenon – is governed by the law of supply and demand and by the law of comparative advantages (see Tesón 2008, 902).

[22] Many authors (see, for example, Freeman 206; Pritchett 2006), however, criticize that the current wave of globalization includes 'everything but labour.

[23] See e.g. Universal Declaration of Human Rights (10 December 1948), Art. 13 (2); International Covenant on Civil and Political Rights (16 December 1966), Art. 12 (2); European Convention on Human Rights (4 November 1950), Art. 2 (2) Prot. No. 4. An alternative, although nowadays minoritarian, view instead regards emigration as a privilege to be granted by the country of origin, rather than a right to which each individual is entitled (for a discussion, see Risse 2012, 152–166).

[24] For a discussion about 'brain hubs in the United States, i.e. innovation clusters where the average GDP and patents for new technologies are higher, see Moretti (2012, 82–88).

The patterns of 'brain' migration also vary. Brain drain may affect developing countries in favour of developed countries, such as non-OECD countries in favour of OECD countries (see, especially, Docquier, Lohest, Marfouk 2007). However, the phenomenon does also occur among OECD countries, as the experience of outward individual movements in developed nations like Italy and New Zealand conspicuously demonstrates (see Brücker *et al*. 2012, 43–47). Further, brain drain can be caused by a reversal of social and economic conditions or unexpected political decisions occurring within a country, which, apparently, is the case of the brain drain that is greatly feared after the Brexit vote in the United Kingdom (see Fazackerley 2018). Lastly, it should be duly considered that migration patterns are likely to change over time, as demonstrated by the history of Europe during the 20th century, when it went from an emigration to an immigration continent, (see Hatton, Williamson 1994, 533–539).

The brain drain phenomenon is a tangible reality also within the EU, where the free movement of workers is one of the four economic freedoms to which Union citizens are entailed and it is a right guaranteed by Article 45 of the Treaty on the Functioning of the European Union (TFEU).[25] In the EU, reasons at the roots of the brain drain relate, mostly, to wage and employment differentials across the Member States as well as different EU regions. While migration patterns mainly followed an East to West route, from countries of the former Soviet bloc – all joining the EU in 2004 and in 2007 – to Western EU-founding Member States during the first decades of the 2000s, the past few years have instead signalled a clear increase of emigration rates from the South to the North of the Old Continent, especially those involving highly-skilled individuals.[26]

Quite intuitively, individual migration patterns also have a significant impact on fiscal revenues. Emigration of individuals, especially

[25] Notably, Article 45 TFEU stipulates that 'freedom of movement for workers shall be secured within the Union', which entails, *inter alia*, the right 'to move freely within the territory of Member States'. EU law, in fact, guarantees both the right of an individual to leave his Member State of origin and the right to enter and live in another Member State. Therefore, freedom of movement of workers is related to the emigration country as well as to the immigration country, both of which are indeed precluded from hindering cross-border movements and discriminating workers based on their different nationality. However, in so far as tax systems and economic rights arising from the Welfare State of the various Member States differ, the economic consequences of an individual's decision to move from one country to another may well be discouraging, which is an issue that the Commission has long committed to tackling but has failed to address so far (see European Commission 2010).

[26] For a more detailed description of past, present, and future trends concerning migration of highly-skilled individuals within the EU, see European Commission 2018b. On labour migration from Eastern to Western Europe in the past decade, see Atoyan *et al.* 2016.

those talented and highly-skilled, who presumably earn an above average salary, erodes the tax base and dampens fiscal revenue in the country of origin. The situation is exactly opposite for the country of arrival, as it later sees an increase in its own tax base and fiscal revenues (with specific regard to individuals moving from India to the United States, see the economics analysis by Desai *et al.* 2009). It is no wonder, therefore, that some measures of control – particularly, in the form of taxes to compensate or promote development in the 'losing' country, i.e. the country of the 'brain' departure[27] – have long been proposed as a way to restore global or inter-country 'fairness' (see, especially, Bhagwati 1976; Brauner 2010).

Similar considerations apply to the current situation within the EU, where Member States should arguably endeavour to harmonise their own fiscal policies rather than fiercely competing against each other as they actually are (see, in this regard, Alcini, Gros 2019), as clearly shown by the increased number of special tax regimes for incoming individuals enacted by Member States in recent years (for a discussion of these regimes, see Beretta 2019a; Beretta 2019b; Beretta 2017; Arginelli, Avella 2017; Ribes Ribes 2017; Bader, Seiler 2015; Cassiano Neves 2010; van Zantbeek 2010; Roxburgh 2006).

From a tax policy perspective, what is particularly worrying of this growing trend is that countries seems to design these special tax regimes before even understanding the real nature of their own social and economic troubles, thus ending up granting tax benefits to individuals based on rather objectionable – if not constitutionally flawed – criteria (see Kostić 2019a).[28]

4. PENSIONERS ON THE MOVE: RETIRING ACROSS BORDERS

If there is a word that perhaps should be retired nowadays, it would be 'retirement' (see Ezra 2019). Just as individual working lives have changed dramatically over the past several decades, so has the conventional wisdom about retirement. Notably, time and again experts advise to

[27] Measures in this regard may be taken by the country of origin, the country of arrival or, even, adopted as the result of international cooperation (for a discussion, see Kapur, McHale 2005).

[28] Reportedly (see Tax Foundation 2019), as from 1 August 2019, Poland introduced a blunt exemption from income tax for all Poles aged below 26 and earning less than a given annual salary (approximately EUR 22,500) as a measure to induce Polish youth to remain in its territory. For its own account, starting in 2019, Portugal (see República Portuguesa 2019) introduced a special tax regime (called '*Programa Regressar*'), providing a 50% reduction of employment income tax, which is specifically designed to encourage the return of former residents who have fled the country in the last years. Indeed, in this as in other cases, one may well question the *differentia specifica* that may justify providing a special tax treatment based solely on the odd criteria such the age or the former residence of an individual (see Kostic 2019a).

prepare for the 100-year life (see, in this regard, Gratton, Scott 2016), in which the three traditional stages of life – education, work and leisure – are going to be subverted.[29] And indeed, anecdotal evidence indicates that droves of people are already 'unretiring' and going back to work (see Cavendish 2019, 71–99; Harding 2018; Span 2018), being that such a decision is favoured by the shrinking of the working-age population, due to declining fertility rates in nearly all developed countries (see He, Goodkind, Kowal 2016, 15).

The circumstances that such that pensioners are, generally, not only healthier but also wealthier; as a matter of fact, the two major sources of private wealth, i.e. illiquid and liquid assets such as houses and pensions, are steadily in their hands – has also brought emigration within the financial reach of many of them (see Gardiner 2016, 33–39). Moving, therefore, is no longer necessarily a young person's game.[30] Indeed, statistics show that an increasing number of pensioners are retiring in countries other than the ones in which they spent their entire or a substantial part of their working life, staying there for at least a considerable part of the year (see, for example, Cruccu 2018; *KeepTalkingGreece* 2018; Tilbrook 2018; Gehring 2017; ONS 2017; *The Economist* 2017).

Although there is very little research into migration patterns of the elderly population and, indeed, the exercising of the right to free movement across the EU by 'economically inactive' citizens, who have reached their retirement age has received scant attention so far,[31] for those individuals the decision to migrate seems to be favoured by a general loosening of occupational and social ties that normally bind an individual to a certain place of residence during their entire working life (see, in this regard, Pyte, Rahmonov 2019). In the EU, cross-border mobility of pensioners is further encouraged by the obligation imposed by EU law upon Member States to eliminate national restrictions that

[29] Notably, the three stages of life, i.e. education, work and leisure, were first laid down by Harold Entwistle in *Education, Work and Leisure* (Routledge 1970).

[30] Against this background, Young (2017, 3, 16, 40) contends that 'people moving across state lines are young', since 'people move not because they are cold and calculating but because of where their opportunities lie', which, according to that author, is more likely to materialize when a person is still relatively young and is trying to establish a career. Conversely, the propensity to move supposedly decreases when a person reaches the peak of their career, due to a variety of factors, such as growing family responsibilities and the accumulation of human, social and cultural capital in the place where the person has settled.

[31] Nevertheless, one recent groundwork study (see Gehring 2019) has pinpointed three main reasons for a retiree to cross country borders: (1) increased free time and the absence of work obligations, (2) availability of budget flights for most destinations as well as the possibility to rely on distance-shortening technologies such as videocalls, and (3) in the EU, the right to free movement across Member States.

impede or discourage the provision of pension portability without objective justification or that are not proportionate to their own aims.[32]

Although, in principle, the brain drain phenomenon only pertains to highly-skilled individuals of working age, the outbound flow of pensioners – indeed, a ‘drain’, and hence a parallel with the brain drain phenomenon may be established – is also a source of concern for governments and policy makers, in so far as it generates a loss of fiscal revenues for the country of origin and a corresponding gain for the country of arrival, a circumstance that induces countries to tightly compete in offering those individuals the most favourable tax and non-tax conditions (in general, with regard to the fiscal effects of migration by an individual from one country to another, see Beretta 2019a; Betten 1998).

Furthermore, even from a purely intra-country perspective, emigration of pensioners undermines the effectiveness of deferred taxation of pension income and leads those countries to shift the fiscal burden on the young, thus impairing intergenerational fairness (see Redonda *et al.* 2019; Xu 2015, 75–77). Given that private pensions are among the most significant financial assets currently held in the household sector, the importance of pensions as a source of revenue for countries is quite obvious and, indeed, it is expected to also remain significant in the near future (see Gardiner 2016, 33–39).

The background of this discourse is that pay-as-you-go (PAYG) regimes, in the form of compulsory contributions, are still a relevant part of pension regimes, in many countries, as well as in most EU Member States, the most common among those schemes being the EET system (Exemption for the individual contributions, Exemption of the savings and capital market returns accumulated in the pension fund, and Taxation upon disbursement of pension wealth once an individual retires).[33] Under

[32] Indeed, the Commission issued a communication on the elimination of tax obstacles to cross-border provision of occupational pensions in 2001, followed by an update in 2003, and launched several infringement proceedings against a number of Member States in the subsequent years (see European Commission 2001a; European Commission 2001b; European Commission 2003). Among the infringement proceeding launched by the Commission over the years, it is worth pointing out the case against Denmark, which resulted in a decision rendered against that Member State by the Court of Justice of the European Union in 2007 (CJEU, case C-150/04, Commission of the European Communities *v.* Kingdom of Denmark, ECLI:EU:C:2007:69). The lack of pension portability and double taxation of cross-border pension have long been identified as a significant obstacle to cross-border movements and a factor of lost income for EU citizens (for a discussion, see Williams 2001; Gutmann 2001). More recently, a regulation on a pan-European Personal Pension Product (PEPP) was passed by the European Parliament in 2019 (see European Parliament 2019).

[33] There are indeed various types of old-age pensions and all are generally underpinned by three tiers of retirement income, i.e. public, occupational and private, whose quantitative significance however varies markedly across countries as well as

such scheme, pensions become taxable for the first time when benefits start being paid out. Alternatives to the EET system are the ETT system (Exempt contributions, Taxed investment income and capital gains of the pension fund, Taxed benefits) and the TEE system (Taxed contributions, Exempt investment income and capital gains of the pension fund, Exempt benefits), although other combinations are also possible.[34]

While in a closed economy setting the aforementioned pension taxation regime works quite smoothly, the migration of a retired person from one country to another instead creates havoc in such a scheme, in so far as the emigrating person pays no taxes in the country of origin, despite the employment activity and the income thereof to which pension contributions can be traced having generally been made in that country (see Starink 2016, 6–13).

As such, the cross-border aspects of private pensions is characterized primarily by a potential conflict between two distinct elements: (1) the ability of an individual to accrue a pension without impediments during the contribution and accumulation phases, regardless of where one person works or lives, and (2) the tax claim by the country of origin over payments made from pensions accrued under favourable tax provisions upon disbursement (see Kavelaars 2007).

The quasi-contractual argument that lies behind such a claim is evident: the emigrating pensioner has received a tax benefit from his country of origin and, therefore, has a duty – a moral one, at least – to pay it back to the country from which he departs (see Brokelind, Axmin 2017, 261). As a matter of fact, the flow of pensioners and, accordingly, of pension income between two countries could very well not be reciprocal and, in some cases, may represent a relatively substantial net outflow for the country of origin of these elderly migrants (see Staats 2015).

Indeed, this quasi-contractual argument gains further traction if the pension income goes untaxed not only in the country of origin but also in the country of arrival, effectively achieving international double non-taxation. Notably, this situation occurs where the emigrating pensioner

between individuals within a country. Notably, in order to render their pension systems more sustainable over time, countries generally motivate employers and employees to support occupational and private retirements savings with various forms of tax preferences or direct subsidies. For an overview of the current and prospective pension systems at the international level, see OECD 2017a.

[34] According to Dilnot, Johnson (1993, 2), 'three main transactions constitute most private pension schemes and it is these transactions which are the possible occasions for taxation: (1) contributions into the scheme, from employer or employee, (2) income derived from the investment of contributions, and (3) payment of retirement benefits from the accumulated fund'. For a discussion of the various pension taxation regimes in the EU, see Brokelind 2014, which concludes that 'cross-border workers may have a lot to lose compared to non-migrant workers, just because of a lack of simplicity in mixing the systems'.

moves from an EET country to a TEE country, in so far as the differences between the pension taxation regimes that are in place in the two countries in question ultimately lead to double non-taxation of the particular income.[35] Indeed, double non-taxation of pensions may also occur if a tax treaty is in place between the country of origin and the country of arrival and such a treaty follows the OECD Model, but the latter country provides for an exemption or simply does not actually tax the relevant pension income (see Beretta 2019b). This situation can be best understood by reviewing the current regime for taxation of pension income under double tax treaties, which is done in the next section.

5. TAXATION OF PENSION INCOME UNDER TAX TREATIES

Under the current version of the OECD Model Convention on Income and on Capital (2017), pension income from past private employment is addressed in Article 18. This article provides for a single – for some, indeed, 'deceptively simple' (see Brown 2019, para. 1.1.1.)[36] – taxation rule, stipulating that pension and similar remuneration, paid in consideration of past private employment, are taxable only in the state of the individual recipient.[37]

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[35] Notably, double taxation and non-taxation as a result of an individual moving across state borders were dealt with at a seminar during the 2008 IFA Congress in Brussels (see De Broe, Neyt 2009). For an analysis of similar issues in the EU, see European Commission 2016.

[36] Notably, according to Brown (2019, para. 1.1.1.), such 'deceptively simplicity' is related to the fact that Article 18 of the OECD Model 'provides no definition and, of course, no source rule. In fact, unlike most of the other distributive rules in tax treaties, the provision is not limited to pensions that arise in one state and are paid to a resident of the other state'. Lacking a tax treaty definition, pursuant to Article 3 (2) of the OECD Model, the term 'pension' must be interpreted in accordance with the domestic law of the jurisdiction imposing the tax, unless the context requires differently. Furthermore, as long as the OECD Model does not include a specific provision regarding social security benefits or annuities, it might be doubtful whether, in a concrete situation, those items of income fall under Article 18 or not (see, most recently: CJEU, case C-372/18, Ministre de l'Action et des Comptes publics *v.* Mr and Mrs Raymond Dreyer, ECLI:EU:C:2019:206, concerning the actual characterization of contributions paid by an individual resident in France to a Swiss social security scheme). Moreover, since Article 18 of the OECD Model provides for no taxation by the source state, it also does not contain any source rule. Accordingly, the allocation rule contained in Article 18 is not limited geographically, which means that all payments that fall within the definitional scope of Article 18 are governed by such rule, without any regard to where those payments actually 'arise'.

[37] Article 18 of the UN Model indeed contains two alternative provisions, i.e. (A) and (B), for taxation of pension income from past private employment. Notably, these two alternatives reflect very distant tax policies. The first alternative (A) includes a general rule that follows the corresponding OECD Model provision. The second alternative (B), instead, ensures taxation by the state of residence of the recipient and the state of which

As an allocation rule, Article 18 closely follows the residence principle. The taxing rights of the source state are therefore completely disregarded. On the other hand, pursuant to Article 19 (2) of the OECD Model, pension income from past government employment is taxable only in the source country, which is identified as the country where the government services were in fact rendered.[38] Importantly, the OECD Model and double tax treaties in general focus only on the actual disbursement of pension income, disregarding the contribution and accumulation phases.

Historically, taxing rights over private pension income shifted from the source country to the residence country at time of the drafting of the 1946 London Model, under the sponsorship of the League of Nations.[39] The main reason for the overhaul is related to the fact that the same shift occurred for taxation of income from movable capital and that private pensions were ultimately regarded as just a form of income from capital.[40] The new allocation of taxing rights among the source and residence countries indeed gained further confirmation in all subsequent updates of the OECD Model[41] and, eventually, the rule was upheld by ensuing discussions which took place inside the various Working Party Committees through the years.[42]

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the payer is a resident. It is worth noting that both alternatives provide for exclusive taxation of social security payments by the source state.

[38] Blank, Ismer (2015, 252–253) indeed suggest bluntly deleting this provision from the OECD Model, in so far as they argue that 'the paying state principle', on which this provision is based, creates a lot of complexities as well as opportunities for tax arbitrage and that, furthermore, a great deal of simplification could be achieved by providing a single rule that applies to all pensions, from both private and government past employment. Along the same lines, see Lang (2007).

[39] Although it is not entirely clear what was the reason taxing rights over private pension income were allocated to the source state instead of the residence state prior to 1946, it should be noted that the 1927 League of Nations Draft Convention also proposed to extend the treatment that had applied only to public pensions – i.e. taxation by the state from which payment was made – to also include private pensions. The Commentaries to Article 8 of the 1927 Draft Convention (League of Nations 1927, 16 [4130]), in fact, explained this decision by stating that 'it appeared both right and practical that all pensions should be made subject to the same rules'. As it happened, the treatment of private pensions provided under the 1927 Draft Convention had little effect on the drafting of actual tax treaties between countries (see Brown 2019, para. 1.2.1.1.).

[40] See League of Nations (1946, 28 [4348]) reasoning that '[i]n the London Draft, private pensions and life annuities are made taxable in the country of fiscal domicile of the creditor, as in the case of interest from debts'. For a discussion, see Starink (2016, 8).

[41] As recalled by Brown (2019, para. 1.2.2.), in truth, the United Kingdom made an attempt to add a subject-to-tax test to the provision that would have been then included in the 1963 OECD Draft, but it only gained the support of the United States.

[42] See OECD (1973, 6) pointing out that 'the article as it stands does not seem to have given rise to difficulties'.

Despite, as a rule, exclusive source-based taxation displays a number of strengths,[43] four broad justifications are usually found for providing exclusive residence-based taxation of pension income from past private employment. Notably, those reasons relate to:

(1) the ability-to-pay principle, as its concrete assessment depends on the worldwide income of the individual taxpayer and it is assumed that personal and family circumstances of the pensioner are better evaluated by the residence state, which, therefore, is also able to ensure personal income taxation of the individual taxpayer on a net basis.[44] On the other hand, taxation of pensions at source is likely to result in excessive taxation, especially if the source state imposes a final withholding tax on the gross amount of pension payments;[45]

(2) the need to fund expenses associated with an aging population, especially for health, pension and care services available to pensioners, whose costs are to be borne by the residence state (see Kavelaars 2007; Blum 1999, 656–657);[46]

(3) easiness of tax administration by the competent authorities, as long as significant hurdles might arise in the case of individuals who have worked in more than one state, changed residence during their career, or

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43 Notably, the main advantage of exclusive source-based taxation is related to the existence of a clear causal link between pension and private employment income, which implies that it is reasonable to tax pensions, as a manifestation of income subject to a suspensive condition, in the very same country where employment income is also taxed. See UN Model Tax Commentary on Article 18 (2017), para. 11. Noteworthy, exclusive source-based taxation is provided under the multilateral Nordic Convention. See Denmark-Faroe Islands-Finland-Iceland-Norway-Sweden Income and Capital Tax Convention (Nordic Convention) (1996) (as amended through 2008), Art. 18 (1).

44 OECD Model Commentary on Article 18 (2017), para. 17. The Commentaries on Article 18 were amended in the 2005 Update of the OECD Model, following discussions among representatives of Member States at the OECD level (see OECD, 2003). Notably, similar considerations can be found also in the case-law of the CJEU (see e.g. CJEU, case C-279/93, Finanzamt Köln-Altstadt *v.* Roland Schumacker, ECLI:EU:C:1995:31, para. 32).

45 It should be noted, however, that in *Hirvonen* (CJEU, case C-632/13, Skatteverket *v.* Hilkka Hirvonen, ECLI:EU:C:2015:765, para. 49) the CJEU ruled that the refusal by the source state to grant non-resident taxpayers, who obtain the majority of their income from the source state and who have opted for the taxation at source regime, the same personal deductions as those granted to resident taxpayers under the ordinary taxation regime, does not constitute, by itself, a discrimination contrary to EU law, in particular where the non-resident taxpayers are not subject to an overall tax burden greater than that placed on resident taxpayers.

46 In this connection, Kemmeren (2001, 32) draws a distinction between the production of income and its consumption, arguing that payment of consumption taxes provide sufficient compensation for the public services offered to emigrated taxpayers in the new country of residence. This argument, however, is rejected by other scholars (see, especially, Starink 2016, 12).

derived pensions from funds established in a state other than the one in which they worked;[47]

(4) simplification of tax compliance obligations for individual taxpayers, since exclusive residence-based taxation enables emigrated individuals to deal with income tax rules and tax authorities of only one country.[48]

Although exclusive residence-based taxation, as the relevant taxing rule, is mandated by Article 18 of the OECD Model and, as seen, a series of justifications for its adoption can be found, actual tax treaty practice shows that allocating taxing rights to the source state is equally possible.

Notably, a study conducted by the IBFD in 2014 (see Wijnen, de Goede 2014) highlighted that, up until 2013, out of 1,811 tax treaties included in the survey, seven tax treaties concluded between two OECD countries provided for exclusive source-based taxation, whereas 25 of them allocated non-exclusive taxing rights to the source state, limited to a certain percentage, ranging between 10% and 25%. As for tax treaties concluded between an OECD and UN country, 44 tax treaties provided for exclusive source-based taxation, whereas 31 of them allocated non-exclusive taxing rights to the source state, limited to a certain percentage, ranging between 10% and 25%.

The tendency to attribute at least some private pension income taxing rights to the source state is indeed growing, in particular among pension-exporting nations like the northern countries in the EU. Denmark, for instance, terminated its tax treaties with France and Spain in 2009, after repetitive failures to negotiate some form of source-based taxation of private pension income with those countries.[49]

Along the same lines, recent tax treaties concluded between the Netherlands, on the one hand, and respectively, Ireland and Germany, on the other, the latter of which came into effect in 2016 (in contrast, the Dutch-Irish income tax treaty is not yet in force), provide for source state taxation of private pensions exceeding, respectively, EUR 25,000 and EUR 15,000 per annum.[50]

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[47] OECD Model Commentary on Article 18 (2017), paras. 19–19.2.

[48] OECD Model Commentary on Article 18 (2017), para. 20.

[49] Notably, the income tax treaties with Spain and France were terminated by Denmark, effective 1 January 2009. See Dyppel 2011, reporting that ‘from a Danish perspective, it is crucial that future treaties contain provisions resulting in a more balanced allocation of rights to tax pension income ... As neither France nor Spain seems to show consideration for the Danish taxation of pensions as a whole and conclude a new treaty with a provision in line with this view, the Minister does not expect new treaties to be entered into in the near future’.

[50] Ireland-Netherlands Income and Capital Tax Treaty (signed on 13 June 2019, not yet in force), Art. 17 (2); Germany-Netherlands Income Tax Treaty (1 Jan. 2016), Art. 17 (2).

Exclusive residence-based taxation, compounded with the adoption of an EET taxation system of private pensions by most countries, ultimately leads to a 'fairness dilemma'. On the one hand, by bilaterally agreeing to such a regime, the country of origin in fact forgoes all its potential fiscal revenues. On the other hand, the emigrating pensioner is effectively double-taxed if the country of origin tries to close the tax income gap by, for instance, taxing pension contributions, whereas the country of arrival, following the treaty, also taxes the pension benefits upon receipt by the individual (see Genser, Holzmann 2016, 10–15). Indeed, in the EU, this situation is further complicated by the encroachment of the freedom of movement across different Member States to which all EU citizens – including 'economically inactive' ones such as pensioners – are entitled.[51]

Nevertheless, as a result of the growing willingness and capacity of pensioners to move across country borders, maintaining an exclusive residence-based taxation for income from private pensions in double tax treaties has become increasingly problematic.[52] Indeed, if, at time when exclusive residence-based taxation was conceived, the amounts of pensions paid cross-border were relatively small in relation to other types of cross-border payments such as dividends, interest and royalties, so that the costs for the source state of giving up its own taxing rights were not seen that great, this is no longer the case in the current political, social and economic landscape (see Brown 2019, para. 1.1.1).

To add to this problem, in a few cases the residence state provides for a blunt exemption or simply does not tax the relevant pension income.[53] This situation occurs in Portugal, which has a special tax

[51] Indeed, as clarified by the CJEU, first, in *Pusa* (CJEU, case C-224/02, Heikki Antero Pusa *v.* Osuuspankkien Keskinäinen Vakuutusyhtiö, ECLI:EU:C:2004:273, para. 18) and then in *Turpeinen* (CJEU, case C-520/04, Pirkko Marjatta Turpeinen, ECLI:EU:C:2006:703, paras. 13–23), the exercising of an economic activity is no longer a requirement for an emigrant to have treaty standing, as the combination of Union citizenship and the right of residence avails the 'economically inactive' citizen of a right to national treatment in the state of destination and of a right of non-restriction in the state of origin. See also CJEU, case C-300/15, Charles Kohll and Sylvie Kohll-Schlesser *v.* Directeur de l'administration des contributions directes, ECLI:EU:C:2016:361, para. 28.

[52] See OECD Model Commentary on Article 18 (2017), stipulating that '[t]he globalisation of the economy and the development of international communications and transportation have considerably increased the international mobility of individuals, both for work-related and personal reasons. This has significantly increased the importance of cross-border issues arising from the interaction of the different pension arrangements which exist in various States and which were primarily designed on the basis of purely domestic policy considerations. As these issues often affect large numbers of individuals, it is desirable to address them in tax conventions so as to remove obstacles to the international movement of persons, and employees in particular'. For a discussion of movements of pensioners across country borders inside the EU, see Del Sol, Rocca 2017.

[53] Granting an exemption to foreign-source pensions does not necessarily imply the complete forfeiture of fiscal revenues, in so far as a country may well expect an

regime providing for a 10-year exemption for foreign-source pension income.[54] Repeated failures to negotiate a new tax treatment for private pensions by Finland with the Portuguese tax authorities led the Scandinavian state to terminate the income tax treaty with Portugal as from 1 January 2019 (see Ambagtsheer-Pakarinen 2018).

Indeed, the number of variations on and deviations from any of the standard models, or even the alternatives included in the Commentaries to the OECD and UN Models, as well as the circumstance that countries are normally prone to negotiate 'bespoke' provisions combining multiple provisions from the Commentaries on Article 18, or ignore them altogether, indicate the existence of scope for reforming the current tax treatment of pension income under double tax treaties (see Brown 2019, para. 1.1.1).

6. A BLUEPRINT FOR INDIVIDUAL TAX REFORM

6.1. Rethinking individual taxation for the 21st century challenges

There are indeed good reasons to believe that international wars and battles for human capital will intensify in the next few decades. Fast-paced automation combined with the increasing specialization of developed countries in human capital-intensive activities are, in fact, expected to spur the general demand for labour by highly-skilled individuals and, thus, also the extent of the brain drain phenomenon. Also, population ageing along with the growing willingness and capability of pensioners to move across borders are predicted to impose tight budget constraints and, thus, put additional pressure on the Welfare State of most developed countries. Ultimately, the aforementioned two phenomena might be in correlation, in so far as challenges related to an ageing population spur the general demand for workers, especially highly-skilled individuals, from abroad.

Uncontrolled flows of people across borders, being either highly-skilled or elderly individuals, could well increase the extent of strategic tax competition among countries, thus draining the brain and fiscal resources of many nations (see Dagan 2018, 59; Rixen 2011, 449). This

increase in collected revenues through indirect taxation. This is indeed the case of Portugal which, reportedly, experienced a sharp increase of new residents in the last years, largely due to its preferential tax regime for foreign-source pensions (see Wise 2019). As stated, Kemmeren (2001, 32) takes the view that payment of consumption taxes by the emigrated individual in the country of arrival offers sufficient compensation for the public services provided by that country to those individual.

[54] Código do Imposto sobre o Rendimento das Pessoas Singulares (CIRPS) [Portuguese Individual Income Tax Code], Arts. 16 (8–12), 72 (6) and 81 (4–6). For a discussion of the Portuguese special tax regime, see Cassiano Neves 2010.

is even truer inside the EU, given the freedom of movement that workers and Union citizens are entitled to under EU law. As a result of such cross-border movements, wealth gaps between those who leave and those who remain – the former not necessarily being the younger, the latter not necessarily being the older – are also likely to widen.

Against this background, the author submits that a coordination strategy to address the current disarray existing in the realm of individual taxation at the international level is highly desirable and that the allocation rules as provided under current double tax treaties, not only for corporate but also for individual taxpayers, should be duly reconsidered.[55] Accordingly, in the following, various policies and measures that might constitute a blueprint for individual tax reform are analysed and their respective pros and cons are in turn evaluated. Importantly, the ensuing discussion mostly focuses on Articles 18 of the OECD Model and taxation of cross-border pension income from past private employment, the author arguing that such an examination might offer valuable suggestions for rethinking individual taxation on a more general scale. Also worth noting is that the following sections only deal with how the taxing rights between the source and the residence state, i.e. the country of origin and the country of arrival in case of migration of an individual from one country to another, could be allocated, without further discussing how the proceeds resulting from such allocation should be used by the countries concerned. As a further word of caution, given that each of the proposed policies and measures warrants an article of its own, only the main elements and arguments of each are hereinafter delineated.

6.2. Extended residence-based taxation

A first measure to address the current challenges encountered in the field of individual taxation may consist in granting taxing rights to the country of origin of the emigrants, being either highly-skilled or elderly individuals, over income received by those persons while abroad.[56] Notably, the possible strategies that the country of origin may implement in order to protect its own tax base against tax-induced migration of individuals can essentially be divided into three broad categories: (1) exit taxes, (2) extended tax liabilities, and (3) recaptures of previously enjoyed benefits, deductions or deferrals (see De Broe 2002, 23).

[55] For a thoughtful examination and some reconsideration of allocation rules for employment income under tax treaties, in particular with regard to Article 15 of the OECD and UN Models, see Kostíć 2019b.

[56] As a matter of international law (see Norr 1961, 432), countries are free to assert jurisdiction over the worldwide income of an individual abroad, provided that a ‘minimum connection’ or ‘nexus’ exists between the country and the individual or the income concerned.

'Exit taxes' or 'departure taxes' can be summarily described as taxes that the country of origin levies upon a person when they cease to be its resident. It is worth nothing that becoming a resident of the other Contracting State under a tax treaty's tie-breaker rule is, in most circumstances, equated to an expatriation. The primary purpose of an exit tax is to ensure that, following the change of residence by a taxpayer, the income accrued while that person was a resident does not escape taxation altogether because of the excluded or limited taxing rights permitted to the source state (i.e. the country of arrival) under its domestic law or by virtue of tax treaty obligations.

As regards their theoretical design, two main types of exit taxes can be distinguished: namely 'general' and 'limited' exit taxes. General exit taxes are fiscal liabilities imposed on all accrued-but-not-yet-realized income (e.g. capital gains) of the emigrated individual. Limited exit taxes are instead imposed on accrued-but-not-yet-realized items of income from certain types of property, such as income from the alienation of a substantial shareholding.

Exit taxes are quite problematic. By imposing an exit tax, a state might in fact be found in breach of its tax treaty obligations. Indeed, an exit tax in regard to pension rights imposed by the Netherlands was found inconsistent with its tax treaty obligations, which, pursuant to Article 18 of the OECD Model, attributed taxing rights on pension income exclusively to the state of residence of the individual recipient.[57] Exit taxes might also be troublesome in relation to obligations deriving from EU law, in so far as those measures amount to illegitimate restrictions on one or more of the four freedoms (for an introduction to this topic, see Helminen 2019, Chapter 2). Since they are immediately charged to the emigrated individual, exit taxes also present complications in cases of temporary migrations, i.e. where an individual moves from one country to another and remains therein only for a few years, to the extent that the individual taxpayer, once returned, is not able to recover the tax paid to the country of origin upon emigration.[58]

The second type of defensive measures is related to 'extended' tax liabilities or 'trailing' taxes. These are taxes that are levied on income that is not otherwise subject to the country of origin's source rules, accrued to an individual within a given period following his change of residence

[57] See: Hoge Raad, BNB 2009/263, 19 June 2009. However, in a more recent decision (see Hoge Raad, BNB 17/186, 14 July 2017), the Dutch Supreme Court held to be compliant with the country's treaty obligations the law enacted by the Dutch government in response to the 2009 Supreme Court decision, prescribing a 'conservatory assessment' limited to the tax-exempt pension contributions accrued to an individual until emigration. For a comment, see Pötgens, Kool (2018).

[58] See Helminen (2002, 234), submitting that 'a mere temporary emigration of a Finnish national should not trigger limited tax liability in Finland. Only emigration, which may be regarded as final, should trigger limited tax liability'.

(generally, five to 10 years).[59] Following the imposition of a trailing tax, based on an idiosyncratic definition of residence (see Oldman, Pomp 1979, 31), the emigrated individual remains liable for tax on their worldwide income in the country of origin, both on income derived from assets owned at the time of departure and on income accrued to them thereinafter. In contrast to an exit tax, a trailing tax is not assessed at the time of the transfer of residence, but only subsequently, i.e. when the individual actually receives the income thereof.

Indeed, the scholarly proposal to change the order of the tie-breaker rules for individual residence purposes currently used in the OECD Model, by primarily assigning residence to the country where the individual taxpayer has their 'centre of vital interests' rather than 'a permanent home available to him', as is presently the case, can be seen as a sort of extended tax liability or trailing tax also (see Brauner 2010, 250). Further, the use, by a country, of citizenship as the main personal connecting factor for income tax purposes, to the extent that by doing so such country succeeds in taxing its expatriated citizens, leads to the same effects.[60] Ultimately, citizenship may also be used, even if not as the main personal connecting factor, in the context of extended liability provisions, by countries having a residence-based tax system (this is the case of Finland, Hungary and Sweden).[61] While these kinds of constraints to tax-driven expatriation are usually unilateral, nothing prevents a specific provision allowing citizenship-based taxation to be inserted in a double tax treaty. France has followed this route in its double tax treaties with Andorra and Monaco.[62]

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[59] Notably, a Dutch ten-years trailing tax, although in the field of inheritance tax, was at stake in *van Hilten* (CJEU, case C-513/03, Heirs of M.E.A. van Hilten-van der Heijden *v.* Inspecteur van de Belastingdienst/Particulieren/Ondernemingen buitenland te Heerlen, ECLI:EU:C:2006:131).

[60] However, it should be noted that at the present, the United States is one of the few countries that still uses citizenship as the main personal connecting factor (for an overview, see Holm 2014). The only other country that uses citizenship as the main personal connection factor, Eritrea, was in fact condemned by both the UN and the EU for the practice of imposing a 2% levy, named 'Diaspora Tax' or 'Recovery and Rehabilitation Tax', on its citizens permanently living abroad. See: United Nations, Resolution 2023, UN Doc. S/RES/2023, 5 December 2011; European Parliament, Resolution on the Situation in Eritrea, 2016/2568(RSP), 10 March 2016. Past practices by other states (most notably, Mexico and Philippines) to levy income tax based on citizenship were, indeed, largely unsuccessful, mainly due to the difficulties encountered by those countries in enforcing tax obligations on their expatriated citizens (see Pomp 2015).

[61] *Tuloverolaki* 1992 [Finnish Income Tax Act], Sec. 11; *Inkomstskattelag* 1999 [Swedish Income Tax Act], Sec. 7; *Személyi jövedelemadóról szóló 1995. évi CXVII. törvén* 1995 [Hungarian Law on Individual Income Tax], Sec. 3 (2) (a).

[62] France-Monaco Income Tax Treaty (18 May 1963), Art. 7; Andorra-France Income Tax Treaty (2 April 2013), Art. 25 (1) (d). For a discussion of the provisions contained in these two treaties, see Kallergis (2015).

As a potential alternative or in addition to the aforementioned measures, the country of origin may decide to recapture or 'claw-back' benefits, deductions or deferrals previously granted to an individual upon emigration. In this way, the country of origin essentially aims to safeguard its latent taxing rights over an emigrant's income.[63] However, claw-back provisions imposed on income such as pensions are highly problematic, in so far as those measures frequently generate a liquidity shortage for the emigrated individual, who might not have readily or entirely available cash needed to pay the tax assessment concerned. Arguably, such kinds of income recaptures should therefore at least contemplate payment in instalments. Notably, with respect to pension income, a proportionate method of tax remittance might take the form of a withholding on monthly pension payments.[64]

Whether any of the measures discussed above is included in a blueprint for a given tax reform, the establishment of some procedural rules would also be needed. In particular, it would be useful to provide for an effective exchange of information and adequate tax collection mechanism between countries. While imposing a tax on its emigrated individuals, a country is in fact confronted with two kinds of hurdles. First, it must obtain accurate information about the emigrated individual's income in order to assess their tax liabilities and, second, it must collect the amount of tax owed.[65] Indeed, an exchange of tax information can also be useful for the country of arrival, as long as a specific obligation is imposed upon such country to take into account the tax charged by the other state while levying its own taxes on the individual taxpayer.[66]

6.3. Subject-to-tax rule(s)

As it is known, under international tax law states are under no obligation to prevent either double taxation or non-taxation, unless specific provisions to that effect are inserted in a double tax treaty. Subject-to-tax rules fulfil precisely this function, by ensuring that income

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[63] In a sense, previously enjoyed deductions represent a sort of 'tax loan', which must be recouped at a later date. See: Opinion of Advocate General Stix-Hackl, case C-150/04, Commission of the European Communities *v.* Kingdom of Denmark, ECLI:EU:C:2006:357, para. 68.

[64] Interestingly, in their proposal for a 'brain drain tax', Bhagwati, Dellalfar (1973, 96) suggested the tax be collected for 10 years following migration or, preferably, through lifetime payments.

[65] Those kinds of procedural rules are set forth, respectively, in Articles 26 and 27 of the OECD and UN Models.

[66] Noteworthy, such an obligation exists in the EU for exit taxes levied on emigrated corporate taxpayers after the first Anti-Tax Avoidance Directive (ATAD) entered into force in July 2016. See: Council Directive (EU) 2016/1164 of 12 July 2016 laying down Rules against Tax Avoidance Practices that Directly Affect the Functioning of the Internal Market, Art. 5 (5), OJ L 193/1 of 19/6/2016.

is taxed at least by one of the two Contracting States (see Rust 2015, 1624 paras. 34). Seen from this perspective, subject-to-tax rules provide a concrete example of how the single tax principle, i.e. the principle stipulating that the same income is to be taxed once and only once, can act as a coordination mechanism to turn the international tax regime into a more comprehensive one.[67]

The idea underlying subject-to-tax rules is anything but new (for a discussion, see Burgstaller, Schilcher 2004; Lampe 1999). Although not generally recommending that states include subject-to-tax rules in their double tax treaties,[68] the Commentaries to the OECD and UN Models in fact mention time and again the possibility for countries of bilaterally agreeing on a rule according to which the tax relief to be granted by one Contracting State is contingent upon the income being subject to tax in the other Contracting State.[69] It is worth noting that a subject-to-tax rule is also included in the Global anti-Base Erosion (GloBE) proposal unveiled by the OECD in early 2019, which essentially aims to ensure that internationally operating businesses pay a minimum level or 'fair share' of taxes (see OECD/G20 2019b; OECD/G20 2019a).

[67] For a theoretical concept of the single tax principle as a cornerstone of the international tax regime, see Avi-Yonah (2007, 8–10). Gil García (2019) argues that 'single taxation is not pursued by tax treaties but is, rather, a consequence when specific provisions are implemented', such as subject-to-tax rules, whereas Shaviro (2015, 6) points out that the single tax principle can be seen as 'an often useful coordinating device'.

[68] Until 2014, the Commentaries to Article 1 on the OECD Model in fact stipulated that '[g]eneral subject-to-tax provisions provide that treaty benefits in the State of source are granted only if the income in question is subject to tax in the State of residence. This corresponds basically to the aim of tax treaties, namely, to avoid double taxation. For a number of reasons, however, the Model Convention does not recommend such a general provision'. OECD Model Tax Convention Commentary on Article 1 (2014), para. 15. The quoted passages were deleted during the 2017 Update of the OECD Model (see OECD 2017b, 47). It is also worth recalling that the BEPS Action 6 Final Report proposed to add new provisions to Article 11 (Interest), Article 12 (Royalties) and Article 21 (Other Income) of the OECD Model, stipulating that interest, royalties or other income arising in a Contracting State and beneficially owned by a resident of the other Contracting State 'may be taxed in the first-mentioned Contracting State in accordance with domestic law if such resident is subject to a special tax regime' (see OECD/G20 2015, 98). The provisions in question would essentially allow taxation by the source country when there is a preferential tax regime in the residence state and this is defined in the relevant tax treaty. However, the proposed new provisions were not included in any of the aforementioned articles during the 2017 Update of the OECD Model.

[69] See e.g. OECD Model Tax Convention Commentary on Article 13 (2017), para. 21, stipulating that '[a]s capital gains are not taxed by all States, it may be considered reasonable to avoid only actual double taxation of capital gains. Therefore, Contracting States are free to supplement their bilateral convention in such a way that a State has to forego its right to tax conferred on it by the domestic laws only if the other State on which the right to tax is conferred by the Convention makes use thereof'. See also UN Model Tax Convention Commentary on Article 13 (2017), para. 4.

The forms and wordings of subject-to-tax rules contained in the various double tax treaties concluded by countries are indeed manifold. According to relevant literature, one criterion for categorizing such rules is whether the subject-to-tax rule only applies to a certain item of income – thus, resulting in a 'specific' subject-to-tax rule – or whether it applies to all categories of income covered by a double tax treaty – thus, resulting in a 'general' subject-to-tax rule (see Burgstaller, Schilcher 2004).

A specific subject-to-tax rule is envisaged in the Commentaries to Article 18 of the OECD Model (reproduced in the Commentaries to Article 18 of the UN Model), allowing source taxation of pension payments where the residence state does not subject to tax these payments 'under the ordinary rules of its tax law'.[70] The adoption of a general subject-to-tax rule by EU Member States in their double tax treaties was instead proposed by the European Commission in its 2012 Recommendation on Aggressive Tax Planning.[71] Moreover, a general subject-to-tax rule is laid down in Article 26 (2) of the multilateral Nordic Convention.[72] A mechanism ultimately resulting in a similar effect to that of a general subject-to-tax rule – commonly called a 'switch-over clause'[73] – is also envisaged in paragraph 4 of Article 23 (A) of the OECD Model and is related to the exemption method used by the residence state, which is prevented from exempting items of income from tax whether those incomes have not been taxed in the source state.[74]

[70] OECD Model Tax Convention Commentary on Article 18 (2017), para. 15. Notably, the subject-to-tax rule on pension income was added to the OECD Commentaries following the 2003 Discussion Draft on Tax Treaty Issues Arising from Cross-Border Pensions (see OECD 2003, 6).

[71] See European Commission 2012b. Dourado (2015, 50–51) submits that 'in the current EU context of tax competition and lack of will to harmonize, it is very unlikely that EU Member States would adopt such a subject-to-tax clause, especially regarding intended gaps, aimed at promoting investment abroad or investment in developing countries. Moreover, EU Member States may also be resistant to adopting a general subject-to-tax clause geographically limited to the EU territory. Taking into account free movement of capital, subject-to-tax clauses should ideally be adopted universally or at least in the OECD context, in order to avoid diversion of investment to those States that do not adopt those rules'. Remarkably, thus far, all these predictions have been fulfilled. For a critical analysis of the subject-to-tax rule recommended by the European Commission in 2012, see Marchgraber 2014.

[72] Convention between the Nordic Countries for the Avoidance of Double Taxation with respect to Taxes on Income and on Capital (23 September 1996, as amended through 2018), Art. 26 (2).

[73] See e.g. van Horzen, De Groot (2018), discussing the switch-over clauses included in the EU anti-BEPS rules.

[74] See also OECD Model Tax Convention Commentary on Article 18 (2017), para. 35. By contrast, Rust (2015, 1655 para. 102) considers that the relevant provision 'does not constitute a subject-to-tax clause'.

In actual tax treaty practice, general subject-to-tax rules can be found in several bilateral treaties, such as those signed by Italy with France and Germany or by Austria with Malta and the United Kingdom.[75] Specific subject-to-tax rules concerning pension income from past private employment can also be found in many double tax treaties, for instance those between Cyprus and Switzerland, Denmark and the United Kingdom, Estonia and Serbia, or France and Switzerland.[76]

Although, as stated, subject-to-tax rules are nothing new under the sun and, indeed, can be found in various double tax treaties, no internationally agreed standard has evolved yet. A blueprint for individual tax reform including such measures could thus offer a valuable framework for harmonizing their interpretation and application. It is worth noting that subject-to-tax rules might be particularly useful to address in situations where pension income from past private employment is not taxed in the resident state of the emigrated retiree due to the operation of a preferential tax regime.[77]

However, it should be noted that a subject-to-tax rule, by itself, is not able to tackle situations in which pension income is actually taxed by the residence state, but a preferential tax rate applies.[78] In fact, even the exact meaning of the term 'subject-to-tax' is far from clear and, thus, the answer to this question is very much open to different interpretations, especially in borderline situations.[79] What if, for instance, no preferential regime exists for pension income in the residence state, but such country is a TEE state and therefore it simply does not levy any tax upon

[75] 1989 Protocol of the France – Italy Income and Capital Tax Treaty (5 October 1989), Point 15; Protocol of the Germany – Italy Income and Capital Tax Treaty (18 Oct. 1989), Point 18 (b); Austria – United Kingdom Income Tax Treaty (30 April 1969, as amended through 2009), Art. 2 (2); Austria – Malta Income and Capital Tax Treaty (29 May 1978), Art. 2 (5).

[76] 2014 Protocol Cyprus – Switzerland Income and Capital Tax Treaty (25 July 2014), Point 4 (b); Denmark – United Kingdom Income Tax Treaty (11 November 1990, as amended through 1996), Art. 18 (1); Estonia – Serbia Income Tax Treaty (24 September 2009), Art. 18 (2); France – Switzerland Income and Capital Tax Treaty (9 September 1966, as amended through 2014), Art. 20 (2).

[77] As recalled in section 5 above, this is the case of foreign-source pensions in Portugal.

[78] For instance, as from 2019, Italy has introduced a special tax regime for incoming pensioners to which a 7% substitute tax of the income tax apply (see Beretta 2019b).

[79] See Lang (2004, 111), also noting that 'in some languages, the term 'subject to tax' means the same as 'liable to tax', thus adding further confusion to the interpretation and application of the expression in question'. The general subject-to-tax rule included in the recommendation issued by the European Commission in 2012 was surprisingly short. It only stipulated that 'an item of income should be considered to be subject to tax where it is treated as taxable by the jurisdiction concerned and is not exempt from tax, nor benefits from a full tax credit or zero-rate taxation' (see European Commission 2012b).

disbursement of pension income? Or, even, what if the amount of pension income is below the minimum taxable amount in the residence state so that no actual tax liability arises? Or, further, what if a substitute tax rather than the statutory income tax applies to pension income, so that such levy might be excluded from the scope of a double tax treaty pursuant to Article 2 of the OECD Model?[80] Shall the subject-to-tax rule operate also in those situations? Moreover, in addition to the specific case of an emigrated pensioner, a subject-to-tax rule fails to entirely address the brain drain issue, since no financial compensation is provided to the country of origin of the highly-skilled emigrant if the income that he receives once in the country of arrival is subject to tax therein.

6.4. Exclusive source-based taxation

One may imagine addressing the challenges arising in the field of individual taxation by means of changes to the relevant allocation rules currently provided under double tax treaties. Notably, with regard to pension income from past private employment, this would imply abandoning exclusive residence-based taxation in favour of exclusive source-based taxation.[81]

A proposal to that effect was recently advanced by Genser and Holzmann. Notably, the two authors implore for a coordinated shift from EET to TEE (or TTE) taxation of pension income, since they regard the latter taxation system of pension income better suited for a world of increasingly mobile individuals, than the EET, adopted by most countries (see Genser, Holzmann 2016, 16–23).[82] In their opinion, universal or widespread adoption of TEE (or TTE) taxation of pension income – in their word 'front-load taxation' instead of 'back-loaded taxation' – would prevent revenue losses for the country of origin when the individual taxpayer emigrates, as the income will have already been taxed at the time it was earned, and would also avoid double taxation, as the residence state would be required to exempt the income in question.[83] As an

[80] As it might occur in the case of the substitute tax that applies to incoming pensioners in Italy as of 1 January 2019.

[81] A model provision to that effect is indeed included in the Commentaries to the OECD Model. See OECD Model Tax Convention Commentary on Article 18 (2017), para. 15. It is worth noting that exclusive source-based taxation is also provided under the multilateral Nordic Convention. See the Convention between the Nordic Countries for the Avoidance of Double Taxation with respect to Taxes on Income and on Capital (23 September 1996, as amended through 2018), Art. 18 (1).

[82] See also Schindel, Atchabahian (2005, 40), noting that 'from the point of view of inter-nation equity and efficiency, exclusive or predominant taxation at source is shaping up as the most reasonable basis of taxation'.

[83] A tax levied by the country of origin over the income of the emigrated individual also emerged from international discussion as the most feasible version of the Bhagwati brain drain tax (see Oldman, Pomp 1979, 246–247).

alternative, they also propose that pension taxation by the source state be deferred until the relevant income is effectively disbursed, so that the tax becomes due only at time of disbursement of the monthly pension benefits (see Genser, Holzmann 2016, 20–21).

The most important advantage of applying the TEE (or TTE) rather than the EET system is that cross-border movements of pensioners from one country to another no longer distort inter-country equity. Pension income is, in fact, taxed already at time when contributions to pension systems are not deductible from employment income in the country of origin, so that no recouping of income tax relief is required to restore equity between different jurisdictions once the individual taxpayer leaves their country of origin. A second advantage is related to the administration of the TEE (or TTE) system in contrast to the EET one, in so far as the former method requires no control of correct deductions for pension savings and since, if the TTE system is applied, old-age pension contributions and pension savings do not reduce the income tax base in the country where the relevant income is built up. The third advantage is related to the fact that, since old-age pension benefits to pensioners are tax-free, for the emigrated taxpayers filing income tax returns in the country of origin is not a requirement, even if pension income is received from several sources, possibly located in different countries. Accordingly, there is no need to establish any source rule either.[84]

Exclusive source-based taxation, however, will only work if countries universally adopt the TEE (or TTE) system. If this is not the case, bilateral tax treaty negotiations will be complicated furthermore by the fact that resident pensioners will receive pension benefits from different source countries, so situations may arise where a country that suffered a tax revenue loss from preferential treatment accorded during the contribution and accumulation phases of pension income, is not the source country paying out the pension income and, is therefore, not part of the negotiation process with the residence state. In fact, a consistent solution to this dilemma would require establishing some form of multilateral consent. In this regard, however, the claim made by Genser, Holzmann (2016, 24) that a pan-European decision to move from a EET to a TEE (or TTE) system of taxation of pension income would put pressure on non-European countries to replicate such an approach, so as to avoid revenue shortfalls and double taxation, does not seem sufficiently grounded.

[84] There are indeed three different possible source rules for pensions, i.e. their source may be located: (1) where the fund paying pension income is established, (2) in the state in which employment services were rendered, or (3) in the state in which deductions in respect of the pension have been claimed. See OECD Model Tax Convention Commentary on Article 18 (2017), para. 19.1; UN Model Tax Convention Commentary on Article 18 (2017), para. 13.

It should also be taken into account that exclusive, rather than shared, taxing rights attributed to the source state are likely to bring additional pressure on national governments during tax treaty negotiations (see Starink 2016, 11).[85] A solution to this shortcoming might then be found in granting the source state shared – as opposed to exclusive – taxing rights with the residence state, regarding pension income. This practically implies limited source-based taxation, meaning that the source tax cannot exceed a specified rate, while the residence state is obliged to credit the tax levied by the source state, as similarly provided for dividends and interest, respectively, in Articles 10 and 11 of the OECD and UN Models. And yet, even this solution presents some hurdles, since limited source-based taxation might not actually be sufficient to fully compensate the country of origin for the fiscal revenues forgone as a consequence of the emigration of an individual taxpayer.[86]

6.5. Compensation tax

An alternative to the aforementioned measures may be to leave the current allocation rule (taxing rights over pension income vested solely to the residence state) unchanged, but to provide at least some fiscal compensation to the source state, which should be identified as the country from which pension income payments are made. The ground idea is that the country of arrival is to levy a tax on pension income to fully or partially compensate the country of origin for the revenues forgone following the expatriation of the individual taxpayer, being either a highly-skilled or an elderly individual. Indeed, although abandoned in later versions of the proposal, as it was found difficult to actually enforce, the original Bhagwati tax proposal envisioned a surtax imposed by the country of arrival (see Bhagwati 1972, 44).

A proposal featuring a sort of compensation tax to address the brain drain phenomenon was also advanced more recently in Lister (2017). The key feature of the proposal contained therein is to resort to a tax credit – roughly akin to the foreign tax credit currently available to US citizens living and working abroad[87] – as a means to compensate the countries of origin experiencing a revenue loss following the departure of highly-skilled individuals from their own territory.[88] Specifically, it is proposed

[85] However, Brauner (2010, 163) contends that a 'brain drain tax' can also be implemented by countries bilaterally, through purposive changes to existing double tax treaties.

[86] A model provision to that effect is included in the Commentaries to the OECD Model. See OECD Model Tax Convention Commentary on Article 18 (2017), para. 15.

[87] Internal Revenue Code (IRC), Title 26, Sub. A, Ch. 1, Subch N, Part III, Subpart A, Sections 901–909.

[88] Lister (2017, 75) defines highly-skilled individuals as those who, cumulatively: (1) have received higher education or skills training, (2) whose training or education was

that the country of origin levy an income tax over employment income earned abroad by its emigrated highly-skilled individuals and that the resulting fiscal proceeds, collected by the country of arrival, are credited against employment taxes due in that country, whereas the remainder is returned to the countries of origin of the emigrated individuals, thereby compensating – at least to a degree – those latter countries for the sunk investment made in human capital that has left its territory. Lister (2017, 76) further stipulates that the levying of the compensation tax is to last long enough to fully compensate the country of origin for the lost investment in the highly-skilled individual.

Cases in point can be found in actual tax treaty practice by countries. It is worth noting that under Article 9 of the 2015 Protocol to the double tax treaty concluded between France and Germany, the resident state of the individual recipient of the pension paid out under the statutory social insurance schemes is entailed to tax the income in question, but it must pay back to the state in which the payments arise a 'compensation amount' corresponding to the tax which that state would have charged under its tax laws.[89]

The main advantage of the aforementioned proposal is that it aligns the interests of both the countries concerned, since it provides for shared allocation of taxing rights between the residence and source states and, therefore it also allows shared allocation of tax revenues between the country of origin and the country of arrival. This is consistent with the fact that, arguably, both countries have a legitimate claim to tax the income of the emigrated individual. Another, related advantage is that countries no longer have to strive for exclusive source-based taxation as a means to tackle tax-induced emigration of individual taxpayers from their own territory. Indeed, this very circumstance is likely to significantly smooth tax treaty negotiations between countries. In the context of the brain drain from a developing to a developed country, the further advantage of this proposal is related to the fact that the compensation tax builds upon the administrative capabilities of the developed country (see Lister 2017, 82).

The major concern related to the proposal under discussion are the nature and characteristics of such a 'compensation tax'. If, in fact, the proposed compensation tax is designed to apply separately and on top of income taxes levied by the residence state (i.e. the country of arrival), it might not actually be considered as an income tax covered by a double tax treaty, pursuant to Article 2 of the OECD and UN Models, with the

largely or completely publicly funded, and (3) have left their own country to work in another within a defined number of years after completing their education or training.

[89] 2015 Protocol of the France – Germany Income and Capital Tax Treaty (21 July 1959, as amended through 2015), Art. 9, introducing a new Art. 13c in the text of the Convention.

consequence that the double taxation relief mechanisms provided in the relevant double tax treaty would not apply. Such a compensation tax might be considered as a sort of 'extraordinary tax', i.e. a levy imposed for a limited period – particularly, until the country of origin is fully compensated for the lost investment in the highly-skilled individual – and for certain reasons, provided various circumstances are also met.[90] Another important disadvantage is related to the fact that the implementation of the proposal requires quite a smooth system through which the collected tax is passed on by the emigrated individual's country of arrival to their country of origin. A further drawback is related to the circumstance that an emigrated individual will be at a disadvantage vis-à-vis an individual resident in the country in the same personal and economic circumstances. As such, the compensation tax seems to run contrary to the general obligation of non-discrimination, which is enshrined both in tax treaties pursuant to Article 24 (1) of the OECD Model and at the EU level in Article 18 TFEU, to the extent that taxation of incoming individuals equates to taxation of foreigners by the country of arrival.[91] However, probably the major source of concern is that the actual implementation of the proposal seems utopian at best, since the country of arrival would not only miss out on fiscal revenues, but it would also have to help collect those proceeds, all for the sole benefit of the emigrated individual's country of origin.[92]

6.6. Global minimum tax

The GloBE proposal unveiled by the OECD in early 2019 envisages an international tax regime where MNEs are required to pay, at least, a minimum level of taxes. This practically ensures that a 'global minimum

[90] 'Extraordinary taxes' are also considered in the Commentaries to the OECD and UN Models. Notably, it is stipulated therein that Article 2 'does not mention 'ordinary taxes' or 'extraordinary taxes'. Normally, it might be considered justifiable to include extraordinary taxes in a Model Convention, but experience has shown that such taxes are generally imposed in very special circumstances. In addition, it would be difficult to define them. They may be extraordinary for various reasons; their imposition, the manner in which they are levied, their rates, their objects, etc. This being so, it seems preferable not to include extraordinary taxes in the Article. But, as it is not intended to exclude extraordinary taxes from all conventions, ordinary taxes have not been mentioned either. The Contracting States are thus free to restrict the convention's field of application to ordinary taxes, to extend it to extraordinary taxes, or even to establish special provisions'. See OECD Model Tax Convention Commentary on Article 2 (2017), para. 4. For a discussion, see Ismer, Blank (2015, 15 para. 28).

[91] Based on paragraph 6 of Article 24 of the OECD Model, the prohibition of discrimination, 'notwithstanding the provisions of Article 2', applies to 'taxes of every kind and description', consequently, in principle, also to a 'compensation levy' that is not covered by a double tax treaty.

[92] As admitted by the same proponent of the 'compensation tax' against brain drain illustrated in this section (see Lister 2017, 83).

tax' is ultimately paid by MNEs. A 'global minimum tax' in the field individual taxation may eventually be introduced, mimicking in a way developments occurring in the corporate sector at the international tax level.

A 'global minimum tax' in the individual sector would in fact display a number of strengths. Probably the most important advantage is related to the fact that its worldwide implementation by countries would provide a unique opportunity for meaningful multilateralism, although it does not seem equally feasible to entrust the administration and collection of such global minimum tax to a 'World Tax Organization'[93], as it was notably stipulated under a version of the Bhagwati tax proposal, which assigned such a task to the UN.[94]

A first concern with regard to a global minimum tax is related to its nature and characteristics. In this sense, similar considerations to those presented above with regard to a compensation tax apply. In addition to the issue of devising a robust enough effective tax rate, there is also the issue of establishing the category of persons to be subject to the tax as well as the rules and principles governing the calculation of the tax base. To put it into a perspective: should a global minimum tax be imposed only on highly-skilled and/or elderly individuals or, also on all/other categories of emigrated taxpayers? Notably, what about emigration of individuals from one country to another for a short period – say, two or three years – such as it may occur in the case of academics and students? In fact, the individual motives for a person to reside abroad could also change over time. Furthermore, as regards the calculation of the tax base, should the income tax rules of the country of arrival or those of the country of origin apply? An autonomous set of rules for calculating the tax base could also ultimately be laid down. Another set of concerns is related to the actual implementation of such a global minimum tax. Even if an adequate consensus is built around it and a multilateral framework is then established, implementing such a tax is by no means straightforward, to the extent that this would require a change of bilateral tax treaties. In this sense, it seems far more practical to amend current tax treaties through a multilateral convention. The experience of the BEPS Multilateral Convention (MLI) can provide useful insights in this regard (see OECD

[93] A first plea for a supervising 'World Tax Organization' was famously made by Tanzi (1999). Questioning the actual feasibility of a 'World Tax Organization' as a means to achieve international tax coordination, see Schön (2009), who considers that 'a realistic outlook will be the ongoing use of bilateral treaties, including some regional multilateral conventions which would extend the number of participants but would not change the traditional character of this instrument as such'.

[94] Oldman, Pomp (1979, 44–58), however, also suggest that the United Nations might only promulgate a set of guidelines for the imposition of an 'international brain drain tax', or 'IBDT', by individual countries.

2017c). However, this would again involve a demanding process, involving modification thousands of existing bilateral treaties on the basis of a complex set of options to accommodate many different possible combinations of treaty partner preferences, as a quick glance at the OECD MLI Matching Database clearly shows (see OECD 2019d).

7. CONCLUSIONS

After BEPS, the idea of tax sovereignty, i.e. that national governments have a non-exclusive right to shape their own tax policies completely independently of one another, seems a distant memory at best. In the post-BEPS world, the unconditional sovereign autonomy of countries over tax matters is, in fact, no longer conceivable.

It is unclear, however, whether the new international tax order that the OECD has long envisaged will ultimately lead to more cooperation or, rather, it will bring more competition among countries. A meaningful cooperation would indeed require building-up a global consensus, based on which a tax level playing field would be established among countries. Without such a global consensus, an international tax order would be difficult to shape, since countries would compete against each other in a global strategic game, based on volatile preferences reflecting their political and economic bargaining power rather than on a sound framework of jointly established principles and rules.

If the ultimate outcome of the action undertaken by the OECD is hard to predict, it is clear that the consequences of non-action at the international level are quite dire, in so far as an increasing number of countries would likely introduce unilateral measures to preserve their own tax base. Indeed, several decentralized actions by countries might ultimately produce the dissolution of any sort of international tax regime. Specifically, with regard to migration of individual taxpayers from one country to another, in the absence of any form of cooperation at the international level, bilateral negotiations would likely be stalled and, perhaps, even rolled back by the intrinsic antagonism of the countries concerned, as a result of their opposing budgetary interests.

This would certainly be detrimental not only from an inter-country perspective, but also from an intra-country point of view. As a matter of fact, in the current political, social and economic landscape, welfare-enhancing objectives can only be achieved if the international and national level are considered simultaneously and, possibly, aligned. The author therefore posits that if a new and fairer social contract is to be established at the national level, the terms and the course of the international tax

order should also be more clearly articulated among countries. In this sense, the various policies and measures explored in this article might eventually kick-off discussions on establishing such an international tax order.

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USING TAX POLICY TO ADDRESS BRAIN DRAIN AND DEPOPULATION: THE CASE OF CROATIA

As the end of the Twenty-Tens approaches, there is a growing public consensus in Croatia that the key challenge facing the country is of demographic nature. Put simply, the accession to the European Union (EU) in July 2013 only exacerbated the negative trends regarding the emigration of mostly young and high-skilled workers to other, more developed countries. However, policymakers have hitherto failed to offer a comprehensive set of countermeasures, with tax policy being no exception. Accordingly, it is the aim of this paper to explore possible tax measures the Croatian legislator may employ in tackling the brain drain phenomenon, with special emphasis on highly skilled workers. More specifically, starting from the assumption that policymakers want to assume a more proactive role in addressing brain drain, the main contribution of the paper is in drawing the contours of a coherent tax-related response to this issue.

Key words: *Brain drain. – Tax policy. – Personal income tax. – Preferential tax regimes. – Exit taxation.*

1. INTRODUCTION

“Demographic disaster”, “Croatian exodus”, “Massive immigration worse than in the times of war” – these and similar headlines have appeared frequently in the Croatian media in recent years, painting a dire picture of the demographic trends and related socio-economic challenges the country is faced with at the end of the current decade.[1] While a

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[1] See, for example, *https://www.slobodnadalmacija.hr/novosti/hrvatska/clanak/id/580359/prava-demografska-katastrofa-iz-hrvatske-je-iselilo-cak-26-puta-vise-ljudi-nego-*

number of forces underlie these developments, it is beyond doubt that the Croatian accession to the European Union (EU) in July 2013 only exacerbated the problem. Put simply, troves of Croatian citizens have taken advantage of the EU freedom of movement and emigrated to other, more developed Member States, such as Germany and Ireland. While the sheer number of émigrés is staggering – one study puts it at 230.000 in the 2013–2016 period alone (Draženović, Kunovac, Pripužić 2018, 436) – their structure causes even more concerns. Namely, in the post-EU accession period there is a notable increase in the emigration of both younger and highly-skilled people (Knezović, Grošinić 2017, 34). Special concerns relate to the flight of healthcare professionals and experts in other propulsive sectors of the economy, e.g. in the information and communication technology (ICT) sector.

Accordingly, the phenomenon of 'brain drain' – defined as the emigration of skilled and professional workers from a country (Wong 2009, 131) – is a genuine problem, albeit not a completely new one, that Croatian policymakers have to grope with. While the socio-economic implications of brain drain are undeniably deep and rather daunting, there is a general public consensus that hitherto no comprehensive set of policy countermeasures has been offered to this effect. This also applies to the more limited sphere of tax policy, even if cross-country experience confirms that tax instruments may play an important role in addressing international mobility of high-skilled labour (OECD 2011, 124).

In this respect, it has to be noted that the body of economic research confirms that cross-country differentials in individual income taxation play a role in people's location decisions.[2] Moreover, such responsiveness seems to be higher for specific categories of workers, such as high-income earners and people whose human capital is not location-specific (e.g. inventors) (Kleven *et al.* 2019; Muñoz 2019). In any case, contemporary migration literature acknowledges that individual countries often use tax policy to address both outbound and inbound cases of highly-skilled migration. Regarding the former, one may speak of 'protective' or 'defensive' tax instruments, such as an exit tax imposed on the emigrant,

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[2] For an overview see, for example, OECD (2011, 128–129); Kleven *et al.* (2019).

while the latter may be designated as 'offensive' measures, e.g. a preferential tax regime offered to immigrants.[3]

Against this broad backdrop, it is the aim of the present paper to explore possible tax policy measures the Croatian legislator may employ in tackling the brain drain, with the special emphasis on highly skilled workers (HSWs), i.e. individuals with at least a tertiary level of education.[4] More specifically, in Section 2 the paper provides a depiction of migration and demographic trends in Croatia, serving as an illustration of why urgent policy action is warranted. In Section 3 it subsequently provides a general overview of the tax instruments that may be used on the domestic level to tackle the brain drain, allowing for lessons be drawn from cross-country experiences. Presuming that Croatian policymakers want to assume a more proactive role in addressing brain drain, Section 4 proceeds with the analysis of pertinent developments hitherto and proposes future course of action. In doing so, particular attention is paid to the newly proposed preferential tax scheme for 'young workers', which is expected to come into force in 2020. While this tax scheme suffers from serious shortcomings, some building blocks of what the author believes should be a coherent tax policy response to the brain drain are expounded, with the aim to influence future debate. The main outcomes of the analysis are summarized in the concluding section of the paper.

Conversely, the design of a global or multilateral solution to the brain drain phenomenon, which is inextricably tied to cosmopolitan perspectives to tax justice, is beyond the scope of the present paper.[5] While the author shares the view that such an approach is indeed desirable and may offer long-term answers to the most pertinent problems, it is hugely debatable whether it constitutes a truly realistic option under the current framework of international tax governance.

2. CROATIAN BRAIN DRAIN: IS THERE THE NEED FOR SERIOUS ACTION?

While it is beyond the scope of the present paper to analyse the specificities of the Croatian brain drain in great detail, it is undeniable that any "anti-brain drain policy" – including tax measures – has to be informed by at least a basic understanding of the phenomenon. Put simply,

[3] Both sets of measures will be explored in detail below, in Section 3. In doing so, the paper departs from the analytical framework laid out in Berretta (2018).

[4] While there is no ubiquitous definition of HSWs, the present paper departs from the assumption that "highly skilled" actually means "highly educated". See the definitions used by the OECD (2011, 124) and the European Committee of the Regions (2018, 7).

[5] Such is the perspective taken, e.g. by Brock (2015) and Lister (2017).

domestic policymakers have to assess the magnitude of the brain drain, evaluate the main factors that influence the location decisions of Croatian migrants, and estimate the overall socio-economic effects of these dynamics. Therefore, this section proceeds with a brief description of migration and demographic trends in Croatia, serving as an illustration of why urgent policy action is warranted.

At the outset it is vital to note that Croatia has historically – since the 15th century – held the status of an emigration country, due to a combination of economic and political factors (Župarić-Iljić 2016, 16). While the country's favourable geographic position and overall standard of living have traditionally also attracted troves of immigrants, particularly from other countries of South-East Europe (Knezović, Grošinić 2017, 16), the negative net migration balance during the entire 20th century has been estimated at 1.2 million (Gelo, Akrap, Čipin 2005, 70). It is a well-known fact that, among countries of comparable size, Croatia has one of the largest diaspora communities, with more than 3 million Croatian citizens living abroad, compared to a domestic population of around 4.2 million (Knezović, Grošinić 2017, 26–27).

The most recent emigration wave of Croats could be traced down to the beginning of the economic downturn in the country in 2009. The ensuing recession lasted for six years (2009–2014), making Croatia as one of the worst economic performers among EU member states. Unsurprisingly, faced with such dire economic conditions – especially a lack of employment opportunities – a number of citizens opted to leave the country. In fact, official government data compiled by the Croatian Bureau of Statistics (CBS) suggests that the onset of the crisis reversed the trend of positive net migration from the beginning of the 21st century (Draženović, Kunovac, Pripužić 2018, 420). The relatively low and stable rates of negative net migration post-2009 have taken a visible turn for the worse since the Croatian accession to the EU in July 2013, demonstrating clearly that the access to the EU labour market constitutes one of the major drivers of emigration (Župarić Iljić 2016, 16–17).

There has been a lively public debate in Croatia on the exact magnitude of these most recent migration flows. Due to a number of factors, mainly of methodological nature, the official migration statistics issued annually by the CBS have been rejected as unreliable in literature, with a shared view that the real numbers of emigrants are significantly higher.[6] As an illustration, while official data puts the negative migration balance – including the relations with non-EU countries – in the 2013–2018 period at around 100,000 (Croatian Bureau of Statistics 2019a), a recent study based on official data compiled by the destination countries

[6] In this regard, we can refer to a comprehensive account provided in Draženović, Kunovac, Pripužić (2018).

estimates that 230,000 people left for other EU countries in the 2013–2016 period alone (Draženović, Kunovac, Pripužić 2018, 436). The numbers seem ever more worrying when viewed together with the negative trends regarding natural population decrease, with the total number of deaths outnumbering the total number of live births by 106,000 in the 2009–2018 period (Croatian Bureau of Statistics 2019b). In fact, Croatia is one of only ten countries in the world that have experienced both negative natural increase and negative net migration in the current decade (2010–2020) (United Nations 2019, 35), thus fuelling concerns of population decline and ageing. According to the UN's World Population Prospects 2019, in the year 2100 Croatia is expected to number less than 2.2 million inhabitants.[7] Another recent study estimates that by the year 2050 around 45% of the domestic population will be aged 55 years or more (Eurostat 2019a, 15).

Beyond the sheer number of people who have left the country, the recent migration flows raise even more concerns when one takes a look at the structure of émigrés. First, it seems that the average age of emigrants has decreased sharply in the post-EU accession period (Draženović, Kunovac, Pripužić 2018, 420–421). In 2018 around 45% of the emigrants were ages 20–39 (Croatian Bureau of Statistics 2019a). Accordingly, a particular source of concern that most emigrants are in their prime age regarding fertility and work abilities (Župarić Iljić 2016, 23). Second, statistical shortcoming aside, it may be reasonably assumed that the EU accession intensified emigration of highly-skilled labour (Knezović, Grošinić 2017, 34; Jurić 2017, 349). According to the report published by the European Committee of the Regions (2018, 12), in the 2014–2017 period Croatia recorded the second largest increase in the number of highly-educated movers (+46%), i.e. migrants with a tertiary level of education, among the EU member states.

While comprehensive sectoral analyses have been largely absent, anecdotal evidence suggests that the brain drain has had significant effects in the healthcare and medical sector (Župarić Iljić 2016, 23–24). In the 2013–2018 period, 525 doctors aged between 25 and 46 have left the country (Vračić 2018, 7). A recent survey conducted among doctors and other healthcare professionals revealed that more than 50% of the doctors aged 45 or younger are thinking about leaving Croatia.[8] Further concerns relate to the flight of experts in the field of ICT, with the number of these highly-sought professionals leaving the country far exceeding the number

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[7] These detailed projections are available at *https://population.un.org/wpp/Download/Probabilistic/Population/* (last visited 31 October 2019)

[8] The survey was conducted by the Croatian Medical Chamber in September 2019. The data is available at *https://www.hlk.hr/istrazivanje-hlk-cak-60-posto-lijecnika-spremno-povuci-suglasnost-za-prekovremeni-rad.aspx* (last visited 31 October 2019)

of newly graduated ICT experts entering the domestic labour market. Put simply, Croatia is at the losing side of intra-EU migrations linked with the so-called knowledge economy (European Committee of the Regions 2018, 9–14).

Regarding the main drivers of emigration from Croatia, there is an amalgam of different 'push' and 'pull' factors at work (Župarić Iljić 2016, 2–3). A recent empirical analysis confirms that access to the EU internal market has indeed been the main driver of emigration since 2013 (Draženović, Kunovac, Pripužić 2018, 435). However, other important factors include the differentials in short-term economic conditions between origin and destination countries (including, e.g. labour market indicators) as well as the degree of corruption in a country (Draženović, Kunovac, Pripužić 2018, 432–436). The importance of non-economic drivers of emigration is confirmed in a number of other studies. For example, in an analysis of the motives for emigration to Germany – by far the most popular country of destination for Croatian emigrants post-2013 – Jurić (2017) highlights the importance of push factors such as corruption, immorality of political elites and legal uncertainty. This is an important lesson for policymakers, since it calls for a holistic approach to the brain drain phenomenon, beyond pure economics.

In any case, these new migratory trends are usually the topic of public discussion in Croatia in terms of their negative socio-economic effects. Biggest concerns relate to the loss of human capital – particularly young, highly skilled professionals – distortions in the labour market, a decrease in the overall productivity of the economy, and the ensuing pressures on the social safety net (Župarić Iljić 2016, 23). On the other hand, policymakers have to be aware that emigration may also have some positive effects, both in the short and long term. Notably, it is quite possible that emigrants may in due time return to their country of origin, armed with newly acquired knowledge and skills. Thus, the related concepts of 'brain regain' and 'brain circulation' have been long acknowledged in migration literature as potential benefits for the sending countries or regions.[9] Further alleviation of the brain drain problem may come in the form of remittances sent to the country of origin by citizens working abroad. In the case of Croatia, these transfer of money from abroad amounted to almost 2.2 billion USD – or 4.3% of the domestic GDP in 2017 (United Nations 2017, 30).

Finally, it has to be noted that the intra-EU mobility of Croatian workers since the accession in 2013 has been subject to some important limitations, since a total of 13 EU Member States employed transitional restrictions on access of workers from Croatia to their respective labour

[9] For an overview see Brauner (2010, 228–237).

markets.[10] As of July 2018 such restrictions are applied only by Austria, which is traditionally – due to geographic proximity and a variety of historic, cultural and socio-economic causes – an important country of destination for Croatian citizens (Župarić Iljić 2016, 18). This last transitory measure will expire by July 2020, adding to the urgency for domestic policymakers to devise a comprehensive brain drain strategy.

3. TAX POLICY RESPONSES: AN OVERVIEW

While the primary purpose of taxation is raising revenues necessary for the financing of public goods, taxes – or, more precisely, certain elements of a particular type of tax – may also have other purposes.[11] According to Avi Yonah (2006, 22–25), aside from a pure fiscal or revenue-raising goal, modern day taxation has two other main functions – redistribution of income and regulation. The latter entails the usage of taxes with the aim to affect the behaviour of citizens, corporations, and other private sector actors, either by incentivizing some activities or by disincetivizing – or rather penalizing – others. This theoretical framework offers a good backdrop for considering the role of taxation vis-à-vis the international mobility of individuals. Namely, countries may employ various tax schemes with a regulatory aim of influencing location decisions of prospective migrants. These measures should obviously be tailored to the local idiosyncrasies regarding migration flows and the overall socio-economic context, with some countries – like Croatia (see Section 2 above) – being under pressure to act to reverse the negative migration trends, while others – usually developed countries – may use tax measures to utilize the ever-growing global mobility of individuals to their advantage, by attracting international talent with, *inter alia*, a competitive economic and tax climate. Further justification for some of these schemes may be found in the traditional legal and economic principles of taxation, such as the ability to pay principle or the benefits principle.

Tax policy responses to the new reality of mobile highly-skilled workers may be divided into two main groups (Beretta 2018, 7). First, there are ‘protective’ or ‘defensive’ tax measures that may be used by a country of emigration (the ‘sending country’) and that, in the jargon of migration literature, have the effect of a ‘pull’ factor. Put simply, here the

[10] A brief overview of these transitory measures, with their date of expiry, is available at *https://ec.europa.eu/social/main.jsp?catId=1067&langId=en* (last visited 31 October 2019).

[11] This is sometimes referred to in the literature as the ‘instrumentalism’ of tax law. See, for example, Gribnau (2003, 25).

sending country reacts to prospective migration by protecting its tax claims on emigrants' income, encompassing the income accrued but not realized before the relocation and the income emigrants may derive in the future. Accordingly, it is possible to differentiate three main types of defensive measures (Beretta 2018, 11): 1) exit taxes; 2) trailing taxes; and 3) claw-back provisions regarding the tax benefits granted in the previous period.

The second group of tax measures may be labelled as 'offensive', in that they are used to induce immigration of HSWs – which may include the return of previous emigrants – into the country. Such schemes may be labelled as 'preferential tax regimes' or 'tax concessions', since here the country grants some kind of beneficial tax treatment (e.g. reduced tax rate) to a targeted group of mobile individuals (Beretta 2018, 19; OECD 2011, 137–141).

The rest of this section proceeds with an analysis of specific defensive and offensive tax measures targeting brain drain, on the basis of selected comparative examples. Since the goal of this exercise is to draw lessons for particular case of Croatia, of special importance is to explore the legal and economic underpinnings of these schemes.

3.1. Defensive measures

From a purely international tax perspective, the event of an individual's emigration from a country is important since it generally results in the termination of the link (nexus) between that country and the individual providing the legal basis for the imposition of income tax.[12] In other words, the individual ceases to be a tax resident of the origin country and her income is thus placed outside of the ambit of that state's tax jurisdiction. The ensuing revenue loss for the coffers of the state of emigration is yet another concern related to global migration flows of young professionals. On this point, one needs to distinguish between at least two parts of the income that is relocated beyond the jurisdictional reach of the emigration state (De Broe 2002, 23; Beretta 2018, 10): (i) gains accrued but not yet realized before the emigration, including the appreciations of the migrant's assets; (ii) income accrued to the taxpayer post-migration, e.g. income from future employment or investment.

Accordingly, a number of countries have made a sovereign decision to impose some sort of a 'departure tax' (or 'emigration tax'), i.e. a tax triggered by the individual's departure from the country.[13] The main

[12] For a general discussion on the 'income tax nexus' in international tax law see Gadžo (2018).

[13] For terminological nuances and the differentiation between the terms 'exit tax', 'emigration tax' and 'departure tax', see, for example, De Broe (2002, 23–25). Of course,

justification provided in tax literature for such measures relates to the legal fundamentals of taxing cross-border income: the state of departure is free to protect its latent taxing claim over the income that is accrued in its territory as well as extending taxing claim on future revenue streams of ex-residents (De Broe 2002, 23). In the well-known jargon of EU tax law, emigration taxes are *prima faciae* reasonable since they ensure fiscal coherence, at least from the viewpoint of the state of emigration (Terra, Wattel 2012, 955–956). However, for the purpose of a meaningful analysis of the normative merits of such measures, it is useful to clearly separate three main types of departure taxes (De Broe 2002, 23): (i) a general or limited exit tax on the accrued gains; (ii) extended tax liabilities or trailing taxes; and (iii) recaptures of the tax benefits enjoyed pre-departure.

Regarding 'classical' exit taxes, it is self-evident that any taxation of accrued unrealized income – whether it extends to all assets belonging to the expatriate (e.g. in Canada or Australia), or is limited only to specific types of property (e.g. the Dutch regime of taxing 'substantial shareholdings')[14] – acts as a disincentive for migration (Arsenault 2009, 59). However, it is extremely doubtful whether this extra cost of departure will offset the expected benefits of the move and thus influence the location decision (Brauner 2010, 265). Further justification for an exit tax regime may be found in the so-called 'benefits principle', which is one of the two main benchmarks of equity or fairness in the distribution of tax burden among individual taxpayers.[15] Put simply, the imposition of a tax burden on the act of emigration may be justified by the benefits the taxpayer in question has previously enjoyed in the state of departure, including the legal protection of her assets.[16] Indeed, it has been acknowledged in tax scholarship that economic cooperation between society members gives rise to certain mutual benefits; in turn, society members need to accept some distributive obligations, including tax obligations (Gadžo 2018, 208). Such benefits provided by the government and other entities belonging to the public sector include, *inter alia,* a functioning judicial system, protection of property rights, public infrastructure, etc. According to Dietsch (2015, 80–89) this may be labelled as a 'membership principle', demanding that individuals should be liable to tax in a country of which they are member, i.e. countries where they benefit from public services and infrastructure. Against this backdrop, it seems beyond doubt that an emigrant who lived in a country

emigration taxes may be also imposed on corporations and other legal entities, but this is of no relevance for the analysis in the present paper.

[14] For an analysis of Canadian and Dutch exit tax schemes, see Chand (2013).

[15] For a more detailed discussion on the content of tax equity see Gadžo (2018, 200–205), and the sources referred to therein.

[16] This argument has been raised in the U.S. within the debate on the desirability of introducing the tax on expatriates in 2008. See Arsenault (2009, 59).

for a considerable period of time had access to public services and public infrastructure to a reasonable extent, thus making them a member of the society with ensuing distributive obligations. This point is linked to the design of an exit tax scheme in countries that follow the 'look-back' approach (e.g. Denmark, Spain, the Republic of Korea), in that they impose the exit only if the expatriate has lived in the country for a substantial number of years before emigrating (Beretta 2018, 13).

Trailing taxes or extended tax liabilities may be more controversial, since they involve the imposition of tax by the origin state in the taxable years following the taxpayer's departure. Accordingly, while these measures are usually discussed in literature as burdening assets previously connected with the territory of the origin state (De Broe 2002, 29–30; Chand 2013, sec. 2.3), they may also be imposed on the streams of income resulting from future employment or entrepreneurial activity in the state of destination.[17] This is in line with some suggestions in the migration literature – epitomized by the so-called 'Bhagwati tax' proposal presented in 1972 – that developing countries, as traditional countries of emigration, should be entitled to a share of the income tax collected on the future income derived by their émigrés (Brock 2015, 52–53). It seems that here the above-discussed benefits argument plays an even more important role than in the case of a classical exit tax. Namely, starting from the assumption that the majority of emigrants are younger, highly skilled individuals[18], one can identify a trove of public benefits provided to them by the emigration country, including the costs of education and training (Brock 2015, 62–63). This may be perceived as a 'sunk investment' that emigration countries may legitimately seek to recuperate, at least partly, by imposing a trailing tax on the former members of their community, i.e. on ex-residents (Brauner 2010, 229). It has to be noted that this type of trailing tax – imposed e.g. on emigrant's future employment income – raises far more concerns from a public international law perspective, since the legal link between the origin state and the taxpayer is less evident. Accordingly, in terms of design features, such schemes often take the form of a 'deemed residence rule', in that the emigrant continues to qualify as a resident of her state of origin post-departure (De Broe 2002, 29–30; Beretta 2018, 15).

Finally, the state of origin may employ the so-called 'recapture' or 'claw-back' rules, i.e. the rules that allow it to recoup, upon the act of emigration, deductions, deferrals and other tax benefits previously granted to the taxpayer in question (Beretta 2018, 18). While in comparative tax systems recapture rules are not that common and are usually linked to a

[17] See Beretta (2018, 15).

[18] This, of course, entails an analysis of the individual countries of emigration. For the case of Croatia see the statistics presented in Section 2 above.

deferred tax schemes (e.g. vis-à-vis pension income), they may be justified, similarly to a classical exit tax, by achieving the overall coherence of a tax system. For the purpose of the present paper it is particularly interesting to note how these measures may be used as a backup for a preferential tax regime granted to highly skilled individuals (see below, Section 3.2).[19]

While the preceding discussion in this Section emphasized the reasons why departure taxes may be justified from a policy perspective, the majority of countries around the globe – including Croatia (see Section 4 below) – have so far abstained from introducing such instruments in their tax systems. Indeed, it is rather easy to identify main policy shortcomings linked to the introduction of an emigration tax. First, it has to be acknowledged that any sort of tax imposed on the event of individual's migration *prima faciae* runs against the basic economic tenet of tax efficiency, in that people's decisions to move across national borders should not be influenced by a barrier in the form of extra tax burden.[20] As pointed out at the beginning of this section, however, tax legislators often put pure economic logic aside having a legitimate regulatory goal in mind. Second, one may find departure taxes questionable from the perspective of tax equity (fairness), since emigrants may feel that their distributive obligations to the country of origin should cease at the moment of departure, with any ensuing increase in the ability to pay belonging to the tax ambit of the destination country. Of even more concern from the fairness point of view is the potential double taxation that may ensue, depending on the interaction between the tax rules of the state of origin and the state of destination (Beretta 2018, 42). Third, departure taxes may involve significant compliance costs for the taxpayer, as well as administrative costs for the tax authorities of the state of origin, particularly in the absence of relevant international agreements in the area of mutual assistance. Fourth, one also has to have in mind the potential advantages flowing to emigration countries from the global mobility of individuals, including the benefits of "brain circulation" (see Section 2, above).

3.2. Offensive measures

Driven by the regulatory goal of inducing highly-skilled individuals to live and work in their own territory, a number of countries employ a specific preferential tax regime provided to this category of (potential) migrants (Kleven *et al.* 2019, 6). This fits well with the competition-based paradigm of international taxation, whereby tax measures are used

[19] For an Italian example in this regard, see Beretta (2018, 18).

[20] On this point in the context of free movement within the EU internal market, see Terra, Wattel (2012, 955).

by states to compete for mobile tax bases (e.g. capital). Put simply, starting from the assumption that wage differentials – which are also affected by the overall tax and social security burden imposed on labour income, i.e. the 'tax wedge'[21] – are one of key drivers of HSWs' location decisions[22], individual countries may offer certain tax incentives for immigration. From a tax-technical perspective, these incentives may take the form of lower tax rates, tax exemptions, tax allowances, deductions, etc. For example, in the year 2010 such incentives were found in tax systems of 16 OECD member states (OECD 2011, 131).

It would be wrong, however, to view preferential tax regimes for HSWs as a policy tool reserved for developed countries. Developing countries may also employ such schemes, either to incentivize return migration, or to increase their overall competitiveness for global talent (Brauner 2010, 266; Del Carpio *et al.* 2016, 2). The latter point is of particular importance today, since no country can ignore the role of human capital in propping up their knowledge-based economy. A good example in this regard is provided by the Malaysian Returning Expert Program (REP). Introduced in 2011, this scheme provides several benefits to Malaysian citizens that have been residing and employed abroad continuously for at least three years prior to application. The benefits granted upon return include a 15% flat tax on employment income, for a period of five years post-return, tax exemptions related to any personal assets the returnee brings into Malaysia, as well as exemption from duties with regard to the purchase or import of a personal vehicle (Del Carpio *et al.* 2016, 7–8). According to data published by the administrative agency in charge of the programme, more than 5,000 individuals have used its benefits in the 2011–2018 period.[23]

The tax concessions provided to HSWs in domestic tax laws may differ considerably in terms of their design. First, it is vital to delimit the subjective scope of the scheme, having in mind the targeted population. While a small group of countries (e.g. Australia, Israel, Spain, United Kingdom) do not demand any skill requirements in order for a migrant to be eligible for the preferential regime, the majority of countries use the so-called targeting provisions, in that the benefits are provided only to migrants possessing certain skill type or level (OECD 2011, 137). Whereas from the administrative perspective it may be simpler to rely on the level of formal education in this regard – e.g. by making the scheme

[21] For its statistical purposes, the OECD defines tax wedge as "(T)he sum of personal income tax, employee and employer social security contributions plus any payroll tax less cash transfers expressed as a percentage of labour costs." (OECD 2018, 576).

[22] See note 2 above, and the accompanying text.

[23] See *https://www.talentcorp.com.my/initiatives/returning-expert-programme* (last visited 31 October 2019).

available to everyone holding a tertiary degree – some countries narrow the subjective scope by targeting specific types of prospective workers. For example, the famous Dutch 'tax ruling scheme', first introduced in 1985, addresses non-residents with professional expertise and skills that are scarce in the Netherlands, including scientific researchers. In a similar vein, Denmark makes its preferential regime available only to scientists and other employees with a salary above the prescribed high threshold (Casarico, Übelmesser 2018, 31–32). It seems that a sort of a hybrid approach is followed in Italy, offering preferential tax treatment both to migrant researchers and other persons with a certain level of education.[24] Conversely, some taxpayers may be explicitly declared ineligible for the scheme, as is the case with professional athletes in Spain (Beretta 2018, 19).

Countries may further rely on criteria such as nationality or (previous) residence to further limit the subjective scope of the preferential regime. Accordingly, in some cases, such as in Israel or in Malaysia (see above in this Section), the scheme is open only to non-resident citizens. A completely opposite approach is followed in other countries (e.g. Belgium, Korea, Netherlands) targeting only foreign nationals (OECD 2011, 143–144). Quite obviously, in light of freedom of movement within the internal market, EU Member States are prohibited from discriminating in this regard against nationals of other EU countries.

Second, regarding the objective scope of the scheme, in most cases only employment income (i.e. a salary) is covered (Beretta 2018, 19–20). However, a broader, more generous approach may be followed, for example extending the benefits to self-employment income and pension income, as is the case in Portugal (Beretta 2018, 20). Due to administrative complexities associated with migration, there are countries that extend preferential treatment also with regard to immigrant's foreign-sourced income (e.g. Australia, New Zealand, Portugal) (OECD 2011, 141; Beretta 2018, 20).

Third, the standard approach is to set the time limitations for preferential tax treatment, thus making it a temporary concession (OECD 2011, 142–143). Time thresholds vary across countries, from two years in Finland to 10 years in Portugal (Kleven *et al.* 2019, 27). In this regard it is worthy to take a look at the historic development of the Dutch scheme, which originally relied on a five-year time threshold. At a later point, the threshold was extended to 10 years, while currently it is stands at eight years. In any case, time restrictions are closely related with potential

[24] Detailed information on the Italian scheme is available at *https://www.agenziaentrate.gov.it/portale/documents/20143/233483/Tax+incentives+for+attracting+human+capital+in+Italy_Tax_incentives_for_attracting_human_capital_in_Italy.pdf/f4a91a80–8ed0–92a5–0186–424a9013bfc3* (last visited 31 October 2019).

policy shortcomings of preferential regimes for HSWs, which is discussed in more detail below.

As already mentioned above, every preferential tax regime for high-skilled workers is primarily a regulatory instrument, in that its main aim is to attract, or retain, targeted individuals in the territory of the given country. This aim is based on the view that there are numerous benefits flowing to the country from an increase in the number of HSWs within its territory. These include, *inter alia*, knowledge-related spillovers increasing the overall level of productivity in the country, positive effects on the labour market in cases of shortages of specific skills, etc. (OECD 2011, 133–134; Casarico, Übelmesser 2018, 31). Put simply, preferential regimes for HSWs constitute a worthy state intervention in order to reap such positive externalities. In this regard it is vital to have in mind the subjective scope of the scheme (see above in this Section), with a number of countries targeting exclusively professionals involved in research and development (R&D) activities.

Likewise, these schemes are a tool of international tax competition, a concept that captures the realpolitik of taxing internationally mobile tax bases, including the labour income of HSWs.[25] In this setting, no country – particularly a small, open economy – can afford to ignore the effective tax burdens in other jurisdiction, and may be forced to reply with its own measures. This seems particularly relevant for high-tax countries and may explicate the introduction of preferential regimes for HSWs in Belgium, Denmark, Finland and Sweden (OECD 2011, 132). Accordingly, some preferential tax schemes may be viewed as having compensatory rather than 'offensive' nature in incentivizing the behaviour of global migrants. Similar logic ostensibly underlies granting beneficial tax treatment to various items that may be categorized as 'costs of migration', e.g. travel costs, additional costs of relocating other family members, etc. For example, one of the justifications provided by the Dutch government in favour of the preferential regime, whereby 30% of qualified employee's gross salary may be paid out as a tax free allowance, is that it provides compensation to foreign professionals for the additional costs related to migration.[26]

Proponents of preferential regimes for HSWs will be also quick in pointing out that their overall fiscal effect for the state of destination tends to be positive, even if the government foregoes some revenue in the

[25] It is beyond the ambit of the present paper to discuss the fundamentals of international tax competition. For an overview see, for example, Faulhaber (2018).

[26] See *https://www.belastingdienst.nl/wps/wcm/connect/bldcontenten/belastingdienst/individuals/living_and_working/working_in_another_country_temporarily/you_are_coming_to_work_in_the_netherlands/30_facility_for_incoming_employees/30_facility_for_incoming_employees* (last visited 31 October 2019).

first step by granting tax concessions (OECD 2011, 134). Put simply, most migrants – particularly HSWs and workers below a certain age – will be net contributors to the tax and social security system of the immigration country.

On the other hand, there is also a number of policy shortcomings linked with the introduction of preferential regimes for mobile individuals. The primary objection comes from the perspectives of equality and equity, which constitute basic legal principles of taxation, usually embodied in national constitutions.[27] It is abundantly clear that giving HSWs preferential tax treatment violates these legal precepts, since one class of taxpayers is put in a privileged position vis-à-vis other members of society (Li 2009, 54). It should be noted that this fundamental criticism may be raised also with regard to other tax expenditures (Gribnau 2003, 25–27). Moreover, the principle of ability to pay dictates in general that the better-off participate more to the financing of public goods, in relative terms. Since the individuals qualifying for preferential regime tend to possess highly sought skills and thus earn above-average income, it is objectionable on the face of it to require these individuals to make lower tax payments than what is mandated by their respective economic faculties (Beretta 2018, 24–25). On the other hand, it is well-understood among tax scholars that legislators have to balance the general normative guidance provided by the principles of tax fairness with other desired objectives of the particular tax measure (e.g. its regulatory goal), meaning that the former may constitute justification to deviate from the latter (Gribnau 2003, 29–30).

Further to this point, critics of preferential schemes often emphasize that their actual behavioural effects are uncertain, meaning that the effectiveness of attracting mobile migrants, as an overarching justification for the introduction of the scheme, is questionable and may be difficult to prove empirically (Li 2009, 54). In other words, due to a number of other factors that affect location decisions, mobile individuals may not respond to the preferential regime as expected by the authorities in the state of destination.[28] Even individuals who decide to relocate to the country may leave when the time limitations of the scheme are reached. In any case, there may be better, less distortive alternatives that pursue similar migration-related goals, including those outside of the ambit of the tax system, e.g. more targeted public investments in education or training (OECD 2011, 136–137).

Finally, it must be accepted that any introduction of a special regime that deviates from the ordinary system of taxation in the country raises the overall level of tax complexity and may therefore bring about

[27] For a general discussion on the importance of these principles in the context of taxation, see, for example, Gribnau (2003).

[28] For an empirical study see Kleven *et al.* (2019).

new administrative and compliance costs. This point is related to the above-discussed design features of a particular preferential regime for HSWs, since it would be difficult to legislate a well-targeted facility in simple legal language (Li 2009, 55).

4. CROATIAN EXPERIENCE AND POTENTIAL POLICY DIRECTIONS

The preceding section provided a general overview of the tax instruments that may be used on the domestic level to tackle brain drain. Against this backdrop, and taking into account relevant tax policy objectives, some lessons from cross-country experiences may be drawn and applied to the particular case of Croatian brain drain, which has been described in Section 2. Since the main aim of the present paper is to explore potential tax policy measures the Croatian legislator may employ in addressing present migration and demographic trends, with a particular emphasis on HSWs, this section proceeds with the analysis of pertinent developments hitherto and proposes building blocks for a new, coherent approach.

As to the last point, it is presumed that Croatian policymakers want to assume a more proactive role in alleviating socio-economic pressures resulting from the troubling rates of immigration of younger, highly-skilled workforce.[29] The following discussion is fruitless and may be dismissed as academic daydreaming if the governing elites continue with a largely passive approach to global migration flows. It must be noted in this regard that Croatia is yet to adopt a new, comprehensive demographic strategy on the national level, even if some of the measures discussed at the level of official expert groups have been leaked to the general public. Admittedly, negative demographic prospects have been explicitly acknowledged and highlighted as one of the major pressure areas in several strategic documents issued recently by the central government (Government of the Republic of Croatia 2019a, 48–49; Government of the Republic of Croatia 2019b, 38–47). However, the envisaged measures for addressing these concerns have been limited to areas such as the institutional support for infants and pre-school children, maternal leave and parental benefits, etc., with no explicit reference being made to the role of taxation (Government of the Republic of Croatia 2019a, 48–49).

Accordingly, it comes as no surprise that none of the measures discussed in Section 3 as tools of anti-brain drain tax policy have been featured in the Croatian tax system since its inception at the beginning of

[29] On the necessity of a more proactive demographic policy in Croatia see, for example, Jurun, Ratković, Ujević (2017).

the 1990s. Even if income is traditionally taxed on a worldwide basis, there has been no serious attempt to employ a departure tax regime for individuals, with the only major tax concern for permanent emigrants being the regulation of their residence status.[30] Such an idea has not come to the fore even though an exit tax will be introduced in the area of corporate taxation, starting 1 January 2020, as a result of the necessity to implement the rules from the EU Anti-Tax Avoidance Directive.[31] Therefore, the Croatian tax system is largely neutral to the act of individuals' emigration from the country – including HSWs – with no special provisions other than the general framework on taxation of income, aimed at disincentivizing such location choices.

Likewise, there are no preferential tax schemes in the Croatian tax system provided to highly-skilled immigrants, including potential returnees. Any immigrant has to take into account the general rules on income taxation in order to determine her tax burden post-migration, including the worldwide-based taxation of resident taxpayers.

4.1. The New Preferential Regime for 'Young Workers': A Well-Intended, but Misdirected Tax Instrument?

Quite interestingly, it was only in 2019 that the capacity of tax policy to respond to migration concerns was explicitly acknowledged. Namely, at the time of writing, a new, migration-related tax measure was in the legislative pipeline: the proposed amendments of the Personal Income Tax Act (PITA)[32], expected to enter into force on 1 January 2020, envisage introduction of the completely new preferential tax regime targeting young workers. More precisely, the proposed benefit takes the legal form of a tax credit in that a fixed percentage is to be subtracted from the tax liability on employment income, calculated under the general rules of personal income taxation. Taxpayers younger than 25 years are to be granted a 100% tax credit, meaning that they will effectively pay no tax on employment income. The second category of beneficiaries are

[30] While the domestic rules on tax residence may be considered similar in nature to 'trailing taxes' (Beretta 2018, 17–18), they are not left out of the analysis in the present paper, since it is difficult to see a genuine connection with the brain drain phenomenon here.

[31] See Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market, OJ L 193 of 19 July 2016. It is interesting to note that Poland made the choice to extend the exit tax provisions of the ATAD also vis-à-vis individuals. See *https://assets.kpmg/content/dam/kpmg/pl/pdf/2018/09/pl-en-tax-alert-KPMG-2018–09–12-taxation-of-unrealized-capital-gains-exit-tax.pdf* (last visited 31 October 2019).

[32] *Official Gazette of the Republic of Croatia*, 115/2016 and 106/2018. The proposed legislative amendments, together with public comments, are available at *https://esavjetovanja.gov.hr/ECon/MainScreen?entityId=12039* (last visited 31 October 2019).

individuals aged 25–30, who are granted a 50% credit in regard to the tax liability on employment income.

In the explanatory text accompanying the bill, the Government explicates the policy underlying this new preferential scheme. In short, by reduction of the tax wedge in regard to young workers' wages, and the corresponding increase in their net disposable income, young and highly-skilled people are given an incentive to stay in Croatia, instead of moving to other countries. Furthermore, the Government explicitly acknowledges the demographic aim of the proposed scheme, without providing any detailed impact assessment or explaining the expected causality.

Evidently, the introduction of this regime is based on the assumption that cross-country wage differentials indeed have a big impact on the location decisions of younger migrants.[33] In terms of the dichotomy between defensive and offensive anti-brain drain tax measures, discussed in Section 3 above, the new scheme displays mostly defensive or protective characteristics. Namely, while it does not impose a new tax burden on individuals' departure from Croatia, as is the case with an exit tax regime, it acts as a tax disincentive to emigration at the expense of the public coffers. In doing so, it is aimed at primarily preserving the existing tax base within Croatia's taxing powers. Conversely, it is difficult to imagine how the new regime may induce immigration to Croatia, particularly due to the relatively low age thresholds limiting its subjective scope. Since the scheme will apply to all workers below the specified age limit, it does not target immigration, including the return of expatriates to Croatia. Quite interestingly, the only other country in Europe that currently applies a similar preferential tax regime for young workers is Poland. Whether the Polish regime – targeting workers below the age of 26, and in effect since 1 August 2019 – inspired the legislative developments in Croatia, remains unanswered at the present time.

The proposed scheme for young workers has been subject to heavy public criticism in Croatia ever since its announcement. First, the predicted behavioural effects of the scheme have been contested from several standpoints. For example, while the Government is apparently convinced of its immediate effects on the level of net salaries, the possibility remains that the reduced tax wedge will be simply soaked up by the employer, thus leaving the net amounts flowing to the employees intact. Even if net salaries do indeed increase as a result of these legislative changes, it is debatable whether its effect will be substantial enough to affect young people's decision on whether to migrate. Namely, it may be reasonably assumed that most young workers, particularly those under the age of 25, have relatively low earnings and are thus not heavily burdened by the personal income tax. Furthermore, a simple calculation shows that an

[33] See above, note 2 and the accompanying text.

individual without children, aged 27 and earning the average salary in Croatia, will experience an increase in the monthly disposable income of around 55 EUR. Such benefit does very little to compensate for huge wage differentials between Croatia and the EU Member States that are most popular destination countries for Croatian migrants (i.e. Germany, Austria, Ireland, Sweden). Moreover, the new regime does not provide any answers to the vexing question of whether beneficiaries will leave the country once the preferential regime expires, i.e. when a person turns 31 years of age. Whether some type of recapture or claw-back rules are warranted in this respect is discussed below (Section 4.2).

The second line of criticism is related to the target of the measure. Due to relatively low age thresholds, the regime does not target the population in the 30–39 age group, even though this segment of the population, in prime age regarding fertility and work, constitutes a large share of the emigrants in recent years (Croatian Bureau of Statistics 2019a). Moreover, it must be noted that, unlike most preferential regimes for immigrants discussed above (Section 3.2), there are no skill requirements for the beneficiaries. If the aim of the scheme is to influence migration decisions of HSWs, then the age thresholds are set rather poorly, since individuals with a tertiary education enter the labour market at the age of 23–24 at the earliest.

Third, is has been suggested that the scheme should be deemed unconstitutional, particularly in light of the constitutional prohibition of discrimination (Article 14 of the Constitution of Croatia)[34] and the principles of equality and equity in taxation, embodied in Article 51 of the Constitution. Regarding the discrimination objection, the envisaged scheme targeted at 'young employees' undeniably causes unequal tax treatment on the basis of age, which is one of the protected grounds of discrimination, even though not explicitly listed in Art. 14(1) of the Constitution.[35] However, on its own, this may not lead to the conclusion on constitutionally prohibited discrimination, since one has to take into account the justifications and policy objectives underlying the rules in question. Namely, the case law of the Croatian Constitutional Court (Ustavni sud Republike Hrvatske) has affirmed that the legislator has a wide margin of appreciation in setting economic and social policy, including tax policy.[36] Accordingly, unequal treatment produced by tax

[34] *Official Gazette of the Republic of Croatia*, 56/90, 135/97, 8/98, 113/00, 124/00, 28/01, 41/01, 55/01, 76/10, 85/10 and 05/14.

[35] However, age is directly referred to among discriminatory grounds in Article 1(1) of the Anti-Discrimination Act (*Official Gazette of the Republic of Croatia*, 85/2008 and 112/2012). More on this, see Omejec (2009, 883–886).

[36] See, for example, decision of the Constitutional Court of the Republic of Croatia, U-IP/3820/2009, 17 November 2009, para. 10. For a general discussion see Bagić (2016, 324–325).

rules may be justified by some legitimate objectives that these rules aim to achieve. As regards various tax benefits – such as the preferential regime discussed here – substantial legislative leeway has been confirmed in the jurisprudence of the Constitutional Court, provided that such provisions are underpinned by reasonable justifications.[37] In other words, tax benefits lay outside of the scope of the constitutional review, as long as they are not arbitrary and unsubstantiated by legitimate policy reasons. Turning attention back to the 'young employees' scheme', it seems clear that while the choice of the age criterion, along with the exact thresholds prescribed in the law. may be derived from the policy perspective, it does not render the scheme entirely arbitrary and thus unconstitutional *per se*. Namely, the claims of the Government that the scheme serves useful social and economic objectives, particularly from the demographic viewpoint, will be probably adjudged by the Constitutional Court as rational considerations of a sufficient degree to pass the prospective constitutional review. A similar conclusion may be reached from the perspective of Article 51 of the Constitution.[38] Here the case-law of the Constitutional Court again confirms a wide margin of appreciation left to the legislator in deciding which facts are relevant in regulating the distribution of the tax burden between taxpayers: as long as a rational ground is provided for the tax classification or the differentiation enshrined in the law, corresponding at least partly to the abstract notion of justice, there is no arbitrariness leading to the conclusion that the constitutional principles of equality and equity are infringed.[39] As previously noted, the policy justifications provided in the Government's bill, amending the Personal Income Tax Act regarding the preferential treatment of young workers, are not to be easily dismissed from this perspective inherent to Article 51 of the Constitution.

Finally, there is a familiar concern that the introduction of the special scheme will add yet another layer of administrative complexity to the Croatian tax system, with the greatest burden falling on the small and medium enterprises, acting as employers. As noted in the above discussion on preferential schemes for HSWs (Section 3.2), there is no real way around this argument, since any deviation from the ordinary system of taxation brings forth additional administrative and compliance costs. The tough question for the policymakers then is whether these costs can be justified by the underlying policy objectives of the scheme at hand.

[37] Decision of the Constitutional Court of the Republic of Croatia, U-IP/3820/2009, 17 November 2009, para. 10.

[38] For a general discussion on the Article 51 of the Croatian Constitution, see Arbutina (2012, 1285–1296)

[39] Decision of the Constitutional Court of the Republic of Croatia, U-IP/3820/2009, 17 November 2009, para. 15.4.

To sum up, it is difficult to see how the proposed regime for young employees may be a success story. Its shortcomings from the policy perspective outnumber its potential gains and the Croatian legislator would be well-advised to opt for alternative instruments to tackle brain drain. Most importantly, these measures should form part of a coherent policy, as deliberated below (Section 4.2). On the other hand, one may have sympathy for the policymakers' desire to come up with a quick fix to a conundrum that reaches far outside the ambit of purely tax domain, or even the economic, for that matter. This is an important point to make, since it signals that there is finally an understanding within the governing elites that the time has come to take a more proactive position vis-à-vis migration flows.

4.2. A Look at the Future: The Basic Tenets of a Coherent nti-brain Drain Tax Policy

In conceptualizing potential solutions to the brain drain problem, and proposing a particular path of action to Croatian policymakers, one must have a good grip on the following facts informing the policy debate:

i. The socio-economic underpinnings of emigration and brain drain: In essence, every regulatory tax measure – such as those discussed in the present paper (see above, Section 3) – has to be based on a fundamental understanding of the situation that requires state intervention. In this regard, the main determinants, magnitude, and effects of the Croatian brain drain have been laid out in Section 2 above. It is evident that the problem mainly boils down to younger (i.e. under the age of 40) and highly-skilled people permanently leaving the country, particularly in the post-EU accession period. Emigration of people with tertiary education seems particularly worrying if one takes into account the education and training costs heavily subsidized from the public purse. For example, according to one estimate, 2 billion EUR has been spent by the government on educating people who have emigrated in the 2013–2017 period.[40] Furthermore, emigration concerns seem to be more pressing as regards certain professions, such as healthcare workers, IT experts, and other employees educated in the wider field of Science, Technology, Engineering and Mathematics (STEM). This mostly has to do with the fact that these professionals face lower barriers when entering labour markets in other countries and are especially coveted in those EU Member States that are traditional destinations for Croatian emigrants (e.g. Germany). Special attention has to be paid to the category of so-called knowledge workers. While there is no ubiquitous definition of this term, they generally include

[40] See *https://prviplan.hr/aktualno/koliko-nas-kosta-odljev-mozgova/* (last visited November 1st 2019).

all individuals with "high degrees of expertise, education, or experience, and the primary purpose of their jobs involves the creation, distribution, or application of knowledge" (Davenport 2005, 10). Accordingly, the term encompasses scientists, researchers, engineers, programmers, and other workers whose knowledge is essential in bringing about innovation, having positive spillovers on the economy as a whole. In this respect, it has to be emphasized that Croatia lags behind other EU countries in terms of innovation, being labelled as a "moderate innovator", leaving behind only Bulgaria and Romania (European Commission 2019a, 7). Even more worryingly, Croatia is the worst performing Member State when it comes to exports of knowledge-intensive services and is well below the EU average regarding human resources, i.e. the availability of a high-skilled and educated workforce (European Commission 2019a, 53). The latter finding has been confirmed in the latest Global Competitiveness Report, noting that the skill set of graduates, the percentage of the active population apt in digital skills, and the ease of finding skilled employees all amount to weaknesses of the Croatian economy (World Economic Forum 2019, 176).[41] The orientation to improve the innovation climate in the near future times ahead has been acknowledged by the domestic policymakers, with an explicit reference to the role of relevant human resources (Government of the Republic of Croatia 2019a, 58–62). The attainment of this goal is undoubtedly under threat if the current trends in emigration of knowledge workers continue, with no real policy on how to possibly induce previous emigrants to return to the country.

ii. The fundamentals of the Croatian tax system: It must be acknowledged that any tax measure targeting brain drain has to fit within the domestic framework of taxing income. Accordingly, a deep understanding of the current rules regarding taxable income, computation of the tax base, tax rate schedule, tax exemptions and privileges, etc., is necessary to choose a particular path of action, if any. All of these elements determine the effective tax burden on labour, which is assumed to influence the individuals' location decision. In this respect, it must be noted that the tax wedge on low-wage earners in Croatia stands at 33.7% and is below the EU average (38.2%), but still much higher than in Ireland (24.2%) or United Kingdom (26.1%) (Eurostat 2019b).[42] Even more importantly for the globally mobile knowledge workers, the top marginal tax rate, including statutory personal income tax rate and surcharges, stands at 42.5%, which is higher than the EU average (39.4%) and seems

[41] Compare also the findings on Croatia in Cornell University, INSEAD, WIPO (2019).

[42] It must be taken into account that this indicator measures the tax wedge for an individual without children, earning 67% of the average salary in the country's business sector.

particularly high compared to the top rates in the new Member States, such as Hungary, Poland, Romania, Latvia, and Slovakia (European Commission 2019b, 26). Put simply, while Croatia is definitely not a high-tax country[43], its ordinary system of taxing employment income is not competitive vis-à-vis high earners, with a significant portion of high-skilled workers falling in this category (e.g. IT experts).

iii. Comparative trends with regard to personal income tax and migration-related measures: In the international competition-based setting, domestic legislators must to pay attention to the global developments in order to improve their competitive position for mobile tax bases. Global trends show that a number of countries have introduced changes to their systems of taxing personal income by either cutting nominal rates or narrowing the tax base (OECD 2019). The latter point is particularly important, since base-narrowing reforms are usually underpinned by specific redistribution and regulatory objectives. This logic may also apply to tax measures targeting migrating knowledge workers, such as the preferential regimes discussed earlier in the paper (Section 3.2).

iv. The EU law dimension: Any prospective tax measure introduced at the domestic level should comply with EU law requirements. While the regulation of individual income tax still remains firmly in the hands of national legislators, with a severely limited role of the EU institutions, domestic rules should not run afoul of the primary EU law, i.e. the provisions enshrined in the EU treaties, such as the rights to free movement within the internal market.[44] In this respect, imposition of a departure tax regime (e.g. a *strictu sensu* exit tax) raises more concerns, since it directly impedes the free movement of labour. However, the jurisprudence of the European Court of Justice (ECJ) has confirmed that the imposition of a tax on the act of individual's emigration may be a justified restriction, provided that the design of the scheme passes the proportionality test.[45] On the other hand, the compatibility of preferential tax regimes granted to mobile individuals with EU law, even if objectionable from the internal market perspective, has hitherto not been under serious scrutiny and thus remains a *domaine réservé* of the individual Member States.[46]

[43] According to the latest data compiled by the European Commission (2019b, 15), Croatia ranks 13th in the EU with regard to the overall tax burden (including social security contributions), relative to the domestic GDP. What is particularly striking is that the only new Member State with a higher tax burden than Croatia is Hungary.

[44] For a general overview see Beretta (2018, 40–43).

[45] Further analysis of the ECJ's case-law remains outside of the scope of this paper. See Terra, Wattel (2012, 957–962).

[46] Compare the discussion in Beretta (2018, 47–51).

Against this backdrop, the remainder of this section presents the main policy recommendations reflecting the views of the author on the particular case of Croatia:

i. Introduction of defensive measures, taking the form of either an exit tax *strictu sensu* or a ‘trailing tax’, is not advisable, since the normative disadvantages of such tax schemes outweigh the potential behavioural impacts and other potential justifications (e.g. the benefits principle). Most importantly, the effect of the exit tax regime on the emigration decision would be greatly diminished due to EU law limitations regarding its exact design, rendering the whole exercise an unnecessary waste of tax authorities’ and taxpayers’ resources.

ii. Conversely, there is some merit to introducing special provisions on ‘recapture’ or ‘claw-back’ regarding previously enjoyed tax benefits. This point is particularly important if policymakers decide to employ preferential regimes for young and/or highly-skilled individuals. As seen from the preceding discussion in this section, one such scheme targeting ‘young employees’ is currently in the legislative procedure in Croatia and is expected to come into force in 2020. Since one of the main objections to this scheme is that it fails to address the migration decision of the beneficiaries once they turn 31 years of age, the legislator may decide to back up the scheme with a protective claw-back provision. For example, one could prescribe that the beneficiaries of the scheme who decide to emigrate must repay the amount of benefit previously enjoyed. It has to be noted that in drawing up such a rule, the EU law requirements – particularly ECJ’s case law on exit taxation – must be taken into account. Accordingly, recapture should not in all likeliness entail an order for an intra-EU migrant to immediately repay the full amount of benefits received.

iii. Whether Croatia needs a special, preferential regime for highly-skilled immigrants, including returning expatriates, remains the most difficult question to answer here. While the author believes that other, general tax measures aimed at strengthening Croatian tax competitiveness are more desirable from a purely theoretical perspective, one has to acknowledge that the current state of affairs regarding demography and migration may call for some quicker, even if less than perfect solutions. In the author’s opinion, a well-designed preferential scheme for immigrants and returnee citizens has in any case numerous advantages over the proposed ‘young employees’ scheme. As stated by Brauner (2010, 266), “(...) The basic idea here is to design tax incentives that will encourage behavior beneficial for development in the context of the brain drain. Tax incentives can and should target specific, well-defined, and isolated

behavior." Indeed, if one connects this argument with the Croatian specificities laid out above, it seems that the prospective preferential tax scheme should have a very limited subjective scope. Namely, against the backdrop of the preceding discussion on the importance of innovations for the economic development of the country and the role of knowledge workers in this regard, preferential regime should target only those professionals possessing crucial skills and expertise in increasing the overall level of innovation. Moreover, the situation in the domestic labour market should play a part in defining the targeted population and making tax-relevant classifications. Some comparative practices may lend a hand in this respect, e.g. the Korean scheme targeted exclusively employees in the high-tech sector (OECD 2011, 144). Regarding the objective scope of the preferential scheme, it would be desirable to extend the benefit to both employment and self-employment income earned in Croatia post-immigration, including foreign-sourced capital income that Croatia may have the right to tax, to further increase the attractiveness of the programme. In any case, preferential tax treatment should be temporary, with a five-year limitation seeming reasonable. This is important to mitigate the impact of the scheme on the overall equity of the tax system. As already pointed out above, any new preferential regime should be accompanied by a claw-back rule vis-à-vis the benefits granted to the migrant.[47]

iv. If one stays within the ambit of personal income tax, there are definitely other options, with a more general scope of application, that seem viable in alleviating the migration-related pressures. In this respect it appears that Croatian policymakers are aware of the global trends and recent years have seen a gradual decrease of the effective tax burden on employment income. However, the tax wedge still remains comparably high, particularly for highly-skilled and highly-mobile individuals earning above-average salaries. Accordingly, a reform of the tax rate schedule should be considered in the mid-term. Furthermore, the system of taxing fringe benefits has also been recently reformed, with an increase of tax-exempt amounts.[48] It still, however, remains relatively rigid in comparison with other EU Member States. One legislative change in the right direction, albeit with a limited scope, has come into force on 1 January 2019, with the introduction of a new, more tax-efficient way for companies to provide stock options to their employees.[49] Since stock option models are a standard way of remunerating workers in the most innovative business sectors, e.g. the IT industry, this change may be adjudged as well-targeted for the category of workers generally highly responsive to cross-country wage differentials.[50]

[47] For an Italian example regarding the claw-back rule see Beretta (2018, 18).

[48] For an overview see Pezo (2019).

[49] See Božina, Wagner (2019, 31).

[50] Compare also the discussion in OECD (2011, 142).

v. Furthermore, it must be acknowledged that there are other areas of the tax system with at least indirect effects on migration decisions of the HSWs, mainly by creating a more competitive tax environment for enterprises engaged in the knowledge-based economy. In this respect is has to be noted that one of the measures envisaged in the Government's tax package, currently in the legislative pipeline and expected to come into force next year, relates to the extension of a lower corporate income tax rate (12%) to all enterprises with an annual turnover up to 1 million EUR. It is thus expected that more than 90% of small corporate taxpayers pay this rather competitive tax rate, which also provided an additional stimulus for the development of the knowledge-intensive start-up sector. While the recent changes in the Croatian tax system are aligned with the global trends of steadily reducing tax burdens on labour and capital, there are certainly some specific instruments the legislator may additionally employ in order to improve the investment climate in innovation-based industries. A number of countries have recently expanded the use of R&D tax incentives (OECD 2019). In this respect an interesting example relevant for knowledge workers comes from Italy, which offers tax credits for corporate taxpayers related to the costs of employee training on 'Industry 4.0' topics. Taken at face value, this seems like a good example of how to simultaneously provide tax benefits to enterprises engaged in the new economy and incentivize improvements of the domestic workforce's relevant skills. One can also contemplate whether Croatia needs a 'patent box' or 'intellectual property box scheme', i.e. a preferential corporate tax regime offered to companies engaged in the development of relevant intangible assets.

vi. Finally, one has to understand that taxation has a severely limited role regarding brain drain. A number of studies have shown that young, highly-skilled people emigrate from Croatia driven by various non-economic factors, including, *inter alia*, the perception of corruption within the society (see Section 2 above). This necessarily calls for a further strengthening of the overall institutional framework in the country. In this respect the tax system – however complex it may seem – is only a small piece of a complex socio-economic mosaic that must aim to improve the overall well-being of the population. For example, if one focuses again on the young and highly-skilled, it is pretty evident that reforms in the education system – more aligned with the conditions in the domestic labour market – may have a more far-reaching impact on the reversal of migration patterns in the long run than piecemeal state interventions regarding net disposable income. Perhaps even more importantly, if Croatia wants to not only prevent further outflow of its top talent, but also to reap the benefits of the 'brain circulation' concept, a coherent set of measures aimed at returnee expatriates and their reintegration into society has to be devised (Vračić 2018, 11–14).

5. CONCLUSION

At the end of the Twenty-Tens, Croatian society is at a crossroads: the governing elites have to decide whether to resign themselves to the role of passive onlookers of the current adverse demographic and migration trends – threatening to tear apart the very socio-economic fabric of the country in the long run – or to adopt a more proactive approach and formulate a set of appropriate policy responses, ranging across different pressure areas. The analysis in this paper shows that, unfortunately, the role of taxes and tax policy in this regard has not been seriously acknowledged hitherto, even if many other jurisdictions have reacted to the global migration of individuals by introducing special tax rules at the domestic level. Admittedly, one may note that a turning point was reached in the autumn of 2019, i.e. at the time of writing this paper, when the proposal to introduce a preferential tax scheme for 'young workers' was brought to the legislative process.

Against this background, the present paper tried to lay out potential tax policy responses to the actual brain drain situation in Croatia, with particular emphasis on highly-skilled workers (or knowledge workers). Its main contribution lies in identifying the main building blocks of a coherent anti-brain drain tax policy, on the basis of both cross-country experiences and relevant economic and legal principles of taxation. What emerges from the paper is that while targeted measures, such as a preferential regime for immigrants and/or returnees, may be problematic from a theoretical standpoint – with horizontal measures providing a better long-term alternative – the magnitude and the structure of emigration from Croatia may warrant some sort of a quick-fix solution. Accordingly, it has been suggested that policymakers may opt for the introduction of a preferential scheme for HSWs, with the main design conundrum being how to draw up proper targeting rules. In any case, the author shares the view that such a migration-related tax instrument has numerous advantages over the proposed 'young workers' scheme, mainly due to the extremely uncertain behavioural effects of the latter. Hope remains that the future debate will refine this or some alternative, and possibly more appropriate, policy approach.

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RESTORING THE EU CITIZENSHIP FOR TAX PURPOSES

Citizenship-based taxation has become insignificant due to high mobility of individuals, which are completely detached from their polities. The lack of political, social and cultural bonds of the individual with the states has shifted the focus to the concept of tax residence. This contribution sheds light on the concept of supranational citizenship in clear opposition to the nation-state citizenship, for the purposes of legitimizing levying a tax on EU citizens. The ongoing concept of EU citizenship anchored firstly in the principle of mutual recognition and secondly in the emergence of democratic and pluralist values under the so-called "European way of life," yields certain imbalances and asymmetries derived from a steep distinction between economically active and economically inactive EU citizens. In the author's view, levying a tax upon EU citizens would enhance the demos and solidarity within the current withered EU integration project.

Key words: *Citizenship. – EU law. – Residence-taxation.*

1. INTRODUCTION

In the globalized economy still suffering the post-traumatic effects of the financial crisis, the European Union free movement of persons has allowed individuals to benefit from better job opportunities in different EU Member States. The migration of highly skilled workers from Southern Member States to Northern EU Members looking for a better life is now a common reality in the EU polity.

Such mobility of individuals benefiting from the EU freedom of circulation of persons has provoked a spillover effect in the EU countries.

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On one side, the Member States create incentives to lure individuals and on the other side, they create incentives to "recapture" those who have already left.[1] The EU mobility of workers mirrors the mobility of capital and urge us to rethink in the nexus to allocate taxing rights. Whilst in the past, taxes were physically constrained to the boundaries of the State, the base erosion and profit shifting (BEPS) landscape completely turned the picture upside-down, thereby presenting multinationals the opportunity to cherry pick the most convenient tax regime to channel their investments. The same dynamics concern individuals who are no longer constrained by the physical boundaries of the State to pay their taxes.

Such cross-border mobility and cherry picking has challenged the concept of citizenship, which is traditionally anchored in the strong nexus between the individual and nation-state. Citizenship strongly pleads for membership, for a common status, namely for being accepted and engaged as fully-fledged member of a polity. In the democratic founding of the modern State, the citizens were identified as the taxpayers. Those who are member of the polity are the exclusive ones deciding the levies and taxes to support the public expenditure and to benefit from the taxes collected. Nevertheless, as Schön points out, taxation and representation undergoes serious conflicts between "those who vote on the tax, those who pay the tax, and those who enjoy the spending of the tax" (Schön 2018).[2] Several questions exemplify such conflicts: Why do the States implement redistribution polices to the detriment of certain taxpayers? Is it necessary to finance public goods if the taxpayer is not interested? How does the State defend the taxpayer against excessive or "expropriation" taxation? How does the well-known "race-to-the-bottom", fostered by the States to lure individuals within a tax competition environment, threaten the redistribution policies of the State in favor of poor citizens?

In the field of taxation, the concept of citizenship linked to the nation-state is in clear decay. Citizenship has been largely replaced by the concept of tax residence (Schön 2018, 41; Beretta 2019, 227–260). Only the US and Eritrea still apply citizenship-based taxation. The consolidation of the tax residence to the detriment of citizenship shakes the groundings of the democratic binomial taxation and representation: "It starts from the fact that citizens living abroad are by and large free of tax burdens in their home country but can retain voting rights while resident foreigners have to pay taxes on their worldwide income without enjoying formal participation in the political process.[...] Should voting rights be made

[1] See regimes for High-Net-Worth Individual regime in Italy, the "Sunny Welcome" for EU pensioners in Portugal, the 30% Dutch tax ruling, *rientro dei cervelli* in Italy etc. Beretta, Giorgio (2018) offers a good overview of these policies. The impact of these domestic policies in a EU competition environment should not be disregarded, as noted by Schön, Wolfgang (2003).

[2] On the democracy and taxation conflicts, see Schön, Wolfgang (2018).

dependent on being subject to domestic taxation? Why are foreign resident taxable at all? Should their personal liability to tax be complemented by voting rights or at least by a constitutional principle of non-discrimination vis-à-vis taxpaying citizens?" (Schön 2018, 41). While citizenship is irrelevant in the domestic context, this contribution wonders whether the concept of citizenship, and particularly restoring the binomial citizen-taxpayer, can still play a decisive role in the current EU integration process.

Aside from the EU own resources (VAT and customs duties), the national contributions from the Member States are the largest source for the EU budget.[3] Since the EU lacks of a direct tax on the EU citizens, this contribution poses the following research question: is the "EU citizenship" concept resilient enough to support the levy of an EU tax? Why is a tax needed and not direct contributions from the Member States? Section 2 of this contribution sketches the features of the concept of supranational citizenship in antagonism towards the "nationalistic citizenship". Such a concept of supranational citizenship serves us as a benchmark to measure the current development of the EU citizenship in Section 3. In Section 4, the author supports the claim that levying a tax on EU citizens is needed to enforce not only the democratic channels but also the solidarity principle within the EU polity. Section 5 provides a conclusion.

2. SUPRANATIONAL CITIZENSHIP VERSUS NATIONALISTIC CITIZENSHIP

Despite the disputes and controversies on the content and meaning of citizenship – which go beyond the scope of this contribution – the extensive literature on political theory dealing with the citizenship traditionally boils it down to the relationship between the individual and a *locus* of politics (Dobson 2006, 20; Bauböck 2006 19; Clarke *et al.* 2014, 10). Such a sense of belonging between the individual and the political community comprises rights and duties within the borders of the nation state (Dobson 2006, 21). Citizenship imbued within a nationalistic spirit reflects sentiments of attachment and common identity to a particular ethnic, political or historic group, but at the same time, it has unfortunately fed the politics of exclusion against the non-citizens (Kochenov 2019).

Under this narrative of citizenship, constrained within the boundaries of the nation-state, Beretta conceives citizenship as a jurisdictional tax nexus (Beretta 2019). The fact that there is a genuine or sufficient link between the individual and its community, namely the

[3] See revenue figures in *https://ec.europa.eu/budget/graphs/revenue_expediture.html* (last visited 26 November 2019).

State, justified the emergence of the well-known "benefit principle" and the "ability to pay principle": "taxes are nothing less than the price that individuals must pay for the various benefits that they receive from the state. Alternatively, citizenship as a criterion for a state to impose its jurisdiction to tax can be premised on 'ability-to-pay theory' considerations, suggesting that individuals are bound to pay taxes, as members of a polity, according to a criterion of distributional equity" (Beretta 2019, Section 2, online version). Nowadays, citizenship-based taxation, which is only visible now in the US and Eritrea, has given way to residence-based tax systems. However, in the latter systems, Beretta stills identifies "citizenship footprints", for example in provisions that extend the state's taxing rights over citizens transferring their residence to low-tax jurisdictions or tax havens (Beretta 2019, Section 4, online version), or in the nationality test in tie-breaker rule in article 4 (2) of the OECD MC to determine the tax residence under a treaty. Beretta argues in favor of disentangling citizenship from playing any role in tax matters, and therefore eliminating such "footprints" in allocating taxing rights. The rationale supporting this claim is derived from the current cross-border mobility of individuals, which weakens the sentiment of belonging or membership to a particular community. The use of citizenship by the States becomes simply instrumental in obtaining more revenue, thereby extending their taxing rights over individuals who are no longer active member of the polity.

The cross-border mobility of individuals, together with the technological advancements, not only must deprive citizenship from any tax meaning, as Beretta previously defends, but also the tax residence concept itself has been recently challenged by Kostic as a nexus to allocate taxing rights under article 15 OECD/UN MC (Kostic 2019). The fact that work can be easily exercised "from any place that allows an internet connection" triggers the decay of the current understanding of how employment is exercised and the categories of employer/employee (Kostic 2019, Section 4 Online version). Accordingly, international tax rules must provide for solutions to the so-called *digital nomads* wherein there is no longer a deep personal link with a certain country (permanent home, family).

The above-mentioned recent diagnosis by tax scholars enhances the mobility of individuals as the rationale to get rid of "old categories", such as citizenship or tax residence. However, both proposals are trapped within the borders of the nation-state. Indeed, the cross-border mobility of individuals has revealed the lack of effective political participation of the individual with the state coupled with the lack of historical, cultural or ethnical bonds to such particular polity. At the outset of the 21st century, however, is the individual only member of the state as a polity? Is it

possible to build up a different meaning of "membership" of the individual with a broader polity than the state? The extensive literature in political theory and philosophy has quite profusely put forward new theories of citizenship deprived from the nationalistic spirit (Bellamy 2008; Christodoulidis 1998). A first attempt to overcome the nation-state boundaries can be found in the cosmopolitan understanding of citizenship, enshrined in the works of philosophers such as Nussbaum and Linklater (Nussbaum 1996; Linklater 1999). Whilst in Nussbaum, cosmopolitan citizenship transpires an "allegiance to a moral community made by the humanity of all human beings" (Nussbaum 1996, 5), in Linklater's Habermasian view, cosmopolitan citizenship aims to create "universal frameworks of communication" (Linklater 1999, 37), in which the excluded, vulnerable and dispossessed can find channels to participate and contest in global governance.

Nevertheless, cosmopolitan citizenship faces up severe criticisms as Dobson convincingly points out. Rather than territorial boundaries, the cosmopolitan citizenship still relies on an "extensive membership" beyond the boundaries of the nation-state to cover the inhabitants of the planet as a whole. Such extensive membership lacks of institutional boundaries, which are needed to deliver political input (information, taxation, etc.) and political output (laws, policies, allocation of tasks and resources) (Dobson 2006, 37). In other words, the world – under the cosmopolitan perception – is too big to be singled out as a "polity" in which the citizen participates in the common life of the community. Cosmopolitan citizenship detached from a legal and administrative institutional system simply becomes "a universal ethic", a sort of "generalized disposition to benevolence exercised within discursive civil communities: a mode of sociability" (Dobson 2006, 38).

In rejecting the cosmopolitan citizenship postulates, Dobson inevitably attaches citizenship to a political institutionalization process. Her concept of supranational citizenship conveys the self-definition of the individual in a complex political order.[4] Supranational citizenship refers to a complex set of institutions consisting of organizational bodies, roles and rules in which the individuals have political rights to interact with each other. In this sense, citizenship can no longer be understood as a kind of personal identity derived from membership of an already-existing social group which gives you an privileged status (i.e. exclusive access to

[4] As noted by Dobson (2006, 170),: "[...] conception of supranational citizenship as the institutional embodiment of the active and collective agency of reasonable composite selves in a community of rights, shaping their common and separate destinies under conditions of political equality and mutual recognition and respect. Whatever its territorial scope, insofar as that citizenship consists in effective powers and constitutes a political order conducing to the wellbeing and freedom of individuals, it authorises and justifies the framework of political authority."

a range of "club goods") compared to non-members (Dobson 2006, 44). Supranational citizenship represents a community of rights providing individuals the capacities to shape the context of their lives and promote the freedom and well-being of others. Supranational citizenship requires the existence of relational bonds among the individuals of a polity beyond the nation-state borders, regardless their own identity. In other words, supranational citizenship becomes a status and its substance (activities, tasks, purposes, dispositions, rights, and duties) is derived from the relationship with other individuals within a complex set of institutions forming a polity beyond the nation state (Dobson 2006, 43).

Strumia also reaffirms the political dimension of supranational citizenship, thereby abandoning any reference to an exclusive identity or ethno-cultural affinity (Strumia 2017). She sketches three prongs of the concept of supranational citizenship: "projection of citizenship beyond the state in the context of a non-hegemonic project; articulation of this beyond-state citizenship within the boundaries of a supranational entity pursuing a collective purpose; and reconfiguration of citizenship beyond nationality through a dynamic of mutual recognition of national citizenships" (Strumia 2017, 672). In principle, the EU regional integration project corresponds to the above-mentioned prongs. First, it is a non-hegemonic project under the constitutional pluralism premises;[5] second, it pursues shared collective values and political goals (articles 1–3 Treaty of the European Union, TEU); third, it relies on mutual recognition, which means that every Member State recognizes national citizens of other Member States to some extent as its own (the EU freedoms of movements and the non-discrimination principle).

One may wonder whether the EU citizenship has achieved the three prongs associated with supranational citizenship. Since EU citizenship is an ongoing project, its content is still forming. In the next section, in dealing with the evolution, meaning and challenges of EU citizenship, we will be confronted with contradictions and asymmetries in relation to the second and third prongs proposed by Strumia.

3. THE JANUS-FACED EU CITIZENSHIP

The introduction of the status of EU citizen in the Treaty of Maastricht (Article 20 of the Treaty of Functioning of the European Union, TFEU) represents a key milestone in the progressive abandonment of the conception of EU citizens as mere market-citizens – as dubbed by Ros (Ros 2018; Ros 2017) – who use the EU freedoms of circulation to

[5] On a detailed account of the Constitutional pluralism within the EU level, see the seminal works by Avbelj and Komarek (Avbelj, Komárek 2012).

carry on economic activity. Pursuant to Article 20 and Article 21 of the TFEU, the citizens of the Union have the right to move and reside freely within the territory of the Member States and cannot be discriminated on the grounds of nationality.

Together with the right to move and reside freely, Article 21 codifies the following rights: "[...] b) the right to vote and to stand as candidates in elections to the European Parliament and in municipal elections in their Member State of residence, under the same conditions as nationals of that State; c) the right to enjoy, in the territory of a third country in which the Member State of which they are nationals is not represented, the protection of the diplomatic and consular authorities of any Member State on the same conditions as the nationals of that State; (d) the right to petition the European Parliament, to apply to the European Ombudsman, and to address the institutions and advisory bodies of the Union in any of the Treaty languages and to obtain a reply in the same language."

However, the enshrinement of EU citizenship in TFEU Article 21 – "Every person holding the nationality of a Member State shall be a citizen of the Union. Citizenship of the Union shall be additional to and not replace national citizenship" – still triggers interpretative doubts in the overlapping with the concept of national citizenship. What is the normative content derived from being a European citizen? What is the additional status of being an EU citizen in the overlapping with the domestic nationality? Such normative content is clearly linked to the benefits that either an EU national or third country national can obtain from an EU host country (i.e. social security, residence permit, rejection of expulsion regime in case of criminal cases, etc.). The extent to which these benefits can be granted by the host Member States has experienced an interesting evolution in the case law of the Court of Justice of the EU (CJEU), which has been codified in the Directive 2004/38.[6] In our benchmark of three prongs of supranational citizenship, described by Strumia (Strumia 2017), we can identify the enhancement of the principle of mutual recognition (Section 3.1), on one hand, and the progressive introduction of collective goals and values forming the European way of life (Section 3.2), on the other.

[6] Directive 2004/38/EC of the European Parliament and of the Council of 29 April 2004 on the right of citizens of the Union and their family members to move and reside freely within the territory of the Member States, amending Regulation (EEC) No. 1612/68 and repealing Directives 64/221/EEC, 68/360/EEC, 72/194/EEC, 73/148/EEC, 75/34/EEC, 75/35/EEC, 90/364/EEC, 90/365/EEC, and 93/96/EEC (Text with EEA relevance).

3.1. European Citizenship as Mutual Recognition

3.1.1. Prohibition of Social Tourism: no Economic Burden for the Member States

The Member States have always been reluctant to extend the social assistance benefits to non-nationals. The idea behind was to prevent the migration of individuals to gain access to more favorable social benefits in the host country, under so-called social tourism. Accordingly, the former Directive 90/364 EEC granted the right of residence to nationals of the Member States and family members, provided that they themselves and the members of their families were covered by sickness insurance, in regard to all risks in the host Member State, and had sufficient resources to avoid becoming a burden on the social assistance system of the host Member State during their period of residence.[7]

In Baumbast,[8] the question posed was whether a German citizen who no longer enjoyed a right of residence as a migrant worker in the host Member State (UK) can enjoy a right of residence by direct application of current Article 20 of the TFEU as a citizen of the European Union. The Court ruled that "the Union citizenship is destined to be the fundamental status of nationals of the Member States."[9] The residence in the UK was granted on the following arguments: (1) Mr. Baumbast first, worked and lawfully resided in the host Member State (UK); (2) second, during that period his family also resided in the UK and remained there even after his activities as an employed and self-employed person in the UK came to an end; and (3) he had sufficient economic resources (comprehensive sickness insurance In Germany) so he and his family were no burdens for the public finances of the UK.[10] The requirement of having sufficient resources has been relaxed in successive case law.

In Zhu & Chen,[11] the UK authorities denied the residence permit to a Chinese national and her daughter, who had acquired the Irish nationality because of being born on the island of Ireland. The UK argued that the condition concerning the availability of sufficient resources means that the person concerned (i.e. the daughter) possesses those resources personally and may not use for that purpose those of an accompanying family member. Contrary to this interpretation, the Court held that the minor was covered by the appropriate sickness insurance of the parent who is a third-country national. Therefore, the minor did not become a burden on the public finances of the host Member State (UK), and a right

[7] See this wording in the current article 7 (1) (b) of Directive 2004/38.

[8] CJEU, Case C-413/99, Baumbast, ECLI:EU:C:2002:493.

[9] Baumbast, para. 82.

[10] Baumbast, para. 92.

[11] CJEU, Case C-200/02, Zhu & Chen, ECLI:EU:C:2004:639.

to reside for an indefinite period in that State has to be granted. In recent Bajratari case,[12] the CJEU went a step further to argue that Article 7 (1) (b) of the Directive 2004/38 did not require that the sufficient resources were obtained legally. Such requirement related to the origin of the resources would be disproportionate.[13] The fact that the income obtained was derived from the unlawful employment of his father (a third-country national without a residence card or work permit) was sufficient for not being a burden for the Member State. These Court's findings are quite responsive to the difficult situations immigrants face in the host state, usually working without a proper work permit (Haag 2019).

While in the previous cases there were sufficient resources, the question becomes troublesome in cases wherein the EU national does not have sufficient resources to avoid becoming a burden on the social assistance system of the host Member State. This scenario is carved out from the scope of Article 24 (2) of Directive 2004/38/EC, which does not oblige the Member States to grant social assistance benefits to economically inactive citizens. Hence, it directly requires an interpretation of TFEU articles 20 and 21 coupled with TFEU Article 18, which enforces the principle of equal treatment and, eventually, the non-discrimination principle laid down in Article 20 of the EU Charter of Fundamental Rights.

In Martinez Sierra,[14] Germany's authorities denied a child-raising allowance to a Spanish national who had been lawfully living in Germany since 1984, without interruptions. The Court ruled that "A national of another Member State who is authorised to reside in German territory and who does reside there meets this condition. In that regard, such a person is in the same position as a German national residing in German territory."[15] The same rationale applies in Trojani,[16] in which a French national residing in Belgium without having sufficient resources could not be excluded from the minimum subsistence allowance, since the principle of non-discrimination requires equal access to the social benefits available only to nationals. The moment an EU national becomes a lawful resident of another Member States entitles them to ask for social benefits as if they were nationals of the host state, to meet the principle of non-discrimination.[17] Both cases strictly apply the principle of mutual recognition, thereby nationals of Member States should be treated equally to residents of the other Member States.

[12] CJEU, Case C-93/18, Bajratari, ECLI:EU:C:2019:809.

[13] Bajratari, para. 42

[14] CJEU, Case C-85/96, Martinez Sala, ECLI:EU:C:1998:217.

[15] Martinez Sala, para. 49.

[16] CJEU, Case C-456/02, Trojani, ECLI:EU:C:2004:488, para. 44.

[17] See also 24 (1) of the Directive 2004/38.

The far-reaching consequences of enforcing the mutual recognition principle in Martinez Sierra and Trojani entailed a serious risk of becoming a burden on the social assistance system of the host Member State. Therein, the successive cases limited their scope. For example, the Dano case[18] concerned the denial of social benefits to Ms. Dano and her son, who were Romanian nationals lawfully residing in Germany, but without intention of seeking employment. In the facts of the case, it was stated that Ms. Dano did not work in Germany or Romania, and "there is nothing to indicate that she has looked for a job".[19] While Article 24 (1) of the Directive 2004/38 consolidated the principle of non-discrimination on the grounds of nationality, Article 24 (2) did not oblige the Member States to confer equal treatment to receive social assistance to EU citizens who are not economically active (i.e. seeking employment). Since Ms. Dano was not economically active, Article 24 (1) of the Directive applies. To apply Article 24 (1) of the Directive, Ms. Dano should have had sufficient economic resources in light of Article 7(1)(b) of Directive 2004/38, thereby preventing becoming a burden on the social assistance system of the host Member State. [20] Therefore, the Court concluded that Ms. Dano did not comply with Directive 2004/38.[21] Economically inactive EU nationals can apply for social benefits in the host Member State on equal footing to nationals if they comply with the requirements of Directive 2004/38. In short, inactive economic citizens cannot claim social benefits on equal footing as nationals of the host state.[22] In Alimanovic, the CJEU was quite explicit on asserting that although the assistance awarded to a single applicant "can be scarcely be described as an unreasonable burden for a Member State, [...] the accumulation of all the individual claims which would be submitted to it would be bound to do so".[23]

This restrictive approach is confirmed in the denial of social assistance benefits to job-seekers from EU Member States in the host country. In Vatsouras & Koupatanize,[24] a case concerning Greek nationals looking for jobs in Germany, the CJEU held that job-seekers must be compared to national job-seekers under Article 45 of the TFEU (freedom of circulation of workers) in term of the social assistance to be granted by the host State "only after it has been possible to establish a real link

[18] CJEU, Case C-333/12, Dano, ECLI:EU:C:2014:2358.

[19] Dano, para. 39.

[20] Dano, para. 64.

[21] Dano, para. 66.

[22] Eric Ros. supra 140, n. 27. This finding has been endorsed in cases like CJEU, Case C-67/14, Alimanovic, ECLI:EU:C:2015:597.

[23] Alimanovic, para. 62.

[24] CJEU, Joined cases C-22/08 and C-23/08, Vatsouras & Koupatanize, ECLI:EU:C:2008:201, para. 38.

between the job-seeker and the labour market of that State." In the event that the real link does not exist, due to short period of time looking for a job or the brief period working in the host state, Article 24 (2) of the Directive 2004/38 does not oblige the extension of social assistance benefits to non-national job-seekers.

For those who have economic resources, albeit obtained unlawfully without the work and residence permit, Bajratari does not oblige the Member States to evaluate how those resources were acquired. For those who do not have economic resources (Dano and the successive line of cases), the Court narrowed down the scope of the mutual recognition principle derived from Martinez Sierra and Trojani*,* which extended social benefits to non-economic actors based purely on the non-discrimination principle in EU law under TFEU Article 18. The need to protect the Member State's budget against social tourism justifies the judicial shift and the return to the territorial argument illustrated in "the real link" of Vatsouras & Koupatanize. The more an individual is integrated into the host Member State, the more the citizen is integrated into a Member State, the more they are entitled to social benefits (Azoulai 2014). Nevertheless, the "real link doctrine" leaves in a difficult situation those EU nationals like Ms. Dano, or Greek job-seekers Vatsouras & Koupatanize, who cannot claim any social assistance due to scarce links with the host EU Member States. Hence, they are compelled to return home or to stay in the host Member State, begging for money and sleeping in homeless shelters (Vonk 2014).

3.1.2. Tax Allowances and Deductions Granted to Economically Active Citizens

In the field of taxation, the Court has exclusively dealt with economically active citizens, inasmuch as they are the ones who work and obviously pay taxes. The questions posed to the CJEU could be summarized in the problems associated with allowances and deductions of EU citizens who reside and work in different EU Member States. The analysis performed is driven under the free movement of workers (TFEU Article 45) in combination with the non-discrimination in articles 18 and 21 of the TFEU. Whilst in the former section, the Court handled the "real link doctrine" in relation to access to social benefits in the host country, similar rationale is followed in the direct tax cases to let nationals of a Member State to benefit from deductions and allowances provided by the host country, where the employment is exercised. In the following cases, the mutual recognition emerges behind the reasoning of the CJEU.

In international taxation, resident and non-resident taxpayers cannot be treated equally in terms of allowances and deductions derived from their personal and family circumstances. Resident taxpayers perform their

economic activities and get access to public benefits and services provided by the State of residence. Therefore, only the State of residence is entitled to take into consideration their personal and family circumstances under the ability to pay principle. In case of non-resident taxpayers, they are subject to limited tax liability which is much lower than resident taxpayers on the same amount inasmuch as the source State does not acknowledge their personal and family circumstances. Such principle of international taxation is set aside in confronting the narrative of European integration upheld by the CJEU, thereby still causing perplexity among the tax scholarship (*see*, Vanistendael 1996).

In Schumacker,[25] the Court allowed Mr. Schumacker, who was living in Belgium with his wife and children but working in Germany, to benefit from the German "splitting tariff" on the grounds that "the non-resident receives no significant income in the State of his residence and obtains the major part of his taxable income from an activity performed in the State of employment, with the result that the State of his residence is not in a position to grant him the benefits resulting from the taking into account of his personal and family circumstances." [26] The principle of mutual recognition recognizes that Mr. Schumacker's situation is substantially equal to that of a German resident, and therefore Germany has to take into consideration his personal and family circumstances. In the successive line of cases, Renneberg,[27] Commission v. Estonia,[28] and X[29], the State of source cannot discriminate the non-resident from a different EU Member State when "all or almost all income" is taxed there and the Residence State cannot take into consideration their personal and family circumstances.

Mr. Renneberg, a Dutch national working in Netherlands but residing in Belgium, bought a house subject to a mortgage loan. The Dutch tax authorities denied the deduction of mortgage interest (negative income) since he was a non-resident in the Netherlands. The Court found discriminatory the different treatment between resident and non-resident taxpayers by the Netherlands. The Court rejected the argument put forward by Netherlands, which qualified the dispute as the mere effect of a disparity resulted from the allocation of taxing rights provided under Article 6.1 of Double Tax Convention between the Netherlands and Belgium. While the positive and negative property-related income related to immovable property located in Belgium is attributed to Belgium, the Netherlands is concerned with work-related income.

[25] CJEU, Case C-279/93, Finanzamt Köln-Altstadt/Schumacker, ECLI:EU:C:1995:31.

[26] Schumacker, paras. 36 and 41.

[27] CJEU, Case C-527/06, Renneberg, ECLI:EU:C:2008:566.

[28] CJEU, Case C-39–10, Commission v. Estonia, ECLI:EU:C:2012:282.

[29] CJEU, Case C-283/15, X, ECLI:EU:C:2017:102.

In Commission v. Estonia, an Estonian national who was resident in Finland earned two pensions of similar amount, one derived from her work in Finland and the other derived from her work in Estonia. Since the amount of the Finnish pension was very small and not subject to tax, Finland, as the State of residence, could not take into consideration her personal and family circumstances, nor Estonia which required 75% of the income obtained in Estonia by the non-resident to take into account their personal circumstances.[30] The formula "all or almost of the income" was lowered to 50% (income perceived in Finland as State of residence) and consequently the Court compelled Estonia to take into account her personal and family circumstances since Finland could not.

In X judgment, the Court replaced the Schumacker formula "from all or almost all income" with "major part of the income".[31] Mr. X, residing in Spain where he owned a dwelling, with income from Switzerland (40%) and from the Netherlands (60%) requested the deduction of the negative income derived from its dwelling in the Netherlands since his personal and family circumstances could not be taken into account in Spain due to the lack of resources. The Court reproduced the previous findings to rule on the existence of discrimination since Mr. X could not have his personal and family circumstances taken into account by the Netherlands, where he receives 60%, and Spain, where he lived. Accordingly, the Netherlands must enable Mr. X to apply his personal and family circumstances, in proportion to the share of that income received in the Member State of activity.[32]

The Schumacher line of cases and especially X judgment disregards the income earned in the source State. It does not matter whether it amounts to 75%, 60% or 50%, because what is really crucial is the fact that the residence State cannot take into account the taxpayer's personal and family circumstances. Ros put it clear: "the X judgment stipulates that it is not decisive whether the taxpayer earns all or almost all his income in one Member State but rather if the Member of State of residence is not in a position to take into account his personal and family situation. In that case it is the Member States of activity that should take into account the personal and family situation of the taxpayer proportionally" (Ros 2018, 158). The pro-rata approach in the X judgment is welcome by the CFE insofar as first, it overturns the outcome of Kieback[33] and second, it supports "an open market economy with free competition, an efficient allocation of production factors, tax neutrality, a level playing field, international tax neutrality, the ability-to-pay principle, the direct benefit principle and origin-based taxation" (CFE ECJ Task Force 2018).

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[30] Commission v. Estonia, para. 55.

[31] X, para. 34.

[32] X, paras. 41 and 49.

[33] CJEU, Case C-9/14, Kieback, ECLI:EU:C:2015:406.

In the author's view, this line of cases strengthened the mutual recognition principle within EU citizenship, which basically compels the EU Member State of source to take into consideration the personal and family circumstances of the taxpayers when the State of residence cannot do so due to the lack of taxable income. The mutual recognition stemming from EU citizenship goes beyond the recognition of fundamental economic rights to freely circulate[34] to impose a duty on the Member State of source to take into consideration the personal and family circumstances of the taxpayer. Even fierce critics of the Schumacher's rationale, such as Wattel, who do not endorse the discrimination analysis handled by the Court – in a nutshell, the State of residence does not discriminate because it did not exercise its taxing power – solve the issue under the national treatment principle in EU law: "the source state that should (proportionally) extend to the non-resident the same personal allowances it grants to its own residents earning the same income (national treatment)".[35] Either under discrimination analysis or under national treatment, there is a duty of the Member State of source to treat equally the non-resident taxpayers who work there.

Schumacher's line of cases is not at odds with the reasoning followed by the Court in Marks & Spencer[36] in which the headquarters country must take into account the final losses of the subsidiaries since the Member State of the residence of the subsidiaries cannot. In both scenarios – corporate tax law (final losses) and personal tax law (personal and family allowances) – the CJEU creates new international allocation rules within the EU polity.[37] Likewise, Schumacher is aligned with "the real link" doctrine in cases like Vatsouras & Koupatanize. The more an individual is integrated within the host Member State, in this case by working there, the more they are entitled to the allowances and benefits provided by the host State to its own residents.

The mutual recognition principle does not only operate in the comparison between resident and non-resident taxpayers: the CJEU has stretched its limits to embrace a horizontal comparison of different non-resident taxpayers in Sopora.[38] In this case, the Dutch 30% wage tax

[34] As noted by Ros (Ros 2018, 159): "[...]the market freedoms are no longer instrumental rights, but are rights granted to EU citizens for their owns sake and can, therefore, be considered as fundamental economic rights".

[35] The Court ruled that discrimination arose from the fact that Mr. Schumacher's personal and family circumstances are taken into account neither in the State of residence nor in the State of employment. In Wattel's view, "one cannot define an alleged discrimination by one state by reference to something another state is not doing (Wattel 2015).

[36] CJEU, Case C-446/03, Marks & Spencer, ECLI:EU:C:2005:763.

[37] Smit observed that the CJEU created a new allocation rule on final losses in relation to Marks & Spencer (Smit 2017, 70).

[38] CJEU, Case C-512/13, Sopora, ECLI:EU:C:2015:108.

facility was only applicable to non-residents living outside Netherlands, at a distance of more than 150 kilometers from the border of the given Member State before taking up a job in the Netherlands. Those who did not comply with this requirement prior to taking the job in the Netherlands were required to provide proof of the amount of extra-territorial expenses to be compensated. Mr. Sopora challenged the denial of the beneficial regime, because he was living at a distance less than 150 Km from the Netherlands border. The Court ruled in favor of the horizontal comparison, thereby prohibiting the Netherlands from discriminating the non-resident, provided that the 30% tax wage did not give rise to a net overcompensation in respect of the extraterritorial expenses actually incurred for taxpayers living less than 150 Km from the Dutch border.[39]

3.2. European Citizenship as Common Values and Ideals ("Union Territory")

While the previous line of cases of EU citizenship operates on the basis of mutual recognition, another stream of cases has enhanced EU citizenship as linked to the "Union territory" beyond the domestic borders. In the landmark Ruiz-Zambrano,[40] the Court dealt with an expulsion order in the field of immigration. The Belgium authorities denied a third country national from Colombia residence in Belgium and his work permit and ordered him to leave the country, despite the fact that his children had already received the Belgian nationality and he made clear efforts to integrate into Belgian society. The Court stated that "A refusal to grant a right of residence to a third country national with dependent minor children in the Member State where those children are nationals and reside, and also a refusal to grant such a person a work permit, [...] would lead to a situation where those children, citizens of the Union, would have to leave the territory of the Union in order to accompany their parents. In those circumstances, those citizens of the Union would, in fact, be unable to exercise the substance of the rights conferred on them by virtue of their status as citizens of the Union".[41]

As Azoulai points out, rather than conceiving the territory of the Union as the sum of individual territories of the Member States, the Union territory should be conceived as "a metaphor for a certain conception of the space referred to in Article 2 TEU as 'a [European] society in which pluralism, non-discrimination, tolerance, justice, solidarity and equality between women and men prevail. Following the Court of Justice's reasoning, leaving European territory means not only leaving Europe in the geographical sense; it means leaving a community

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[39] On positive appraisal of the Sopora judgement, see Kemmeren (2015).

[40] CJEU,Case C-34/09, Ruiz Zambrano, ECLI:EU:C:2011:124, para. 44.

[41] Ruiz Zambrano, paras. 43 and 44.

of ideals and values; it means being deprived a certain mode of existence corresponding to the standards of European society. As stated in Ruiz Zambrano, the territory of the Union 'transcends' the 'territorial framework of national communities'. It stands for the mix of material and immaterial things that determines the sustainability of individual existence; what we may call a 'European way of life" (Azoulai 2014, 3).

The Territory of the Union as a space of ideals and values, beyond the Member States' borders, is reaffirmed in Garcia Abello in relation to the surnames.[42] Belgium denied Mr. Garcia Avello and his spouse (Spanish nationals residing in Belgium) the change requested in their patronymic surname of their two children, who were born in Belgium. The justification for the rejection was based on principle of the immutability of surnames as a founding principle of social order to prevent risks of confusion as to identity or parentage of persons.[43] The Court dismissed such justification on the grounds that "parentage cannot necessarily be assessed within the social life of a Member State solely on the basis of the criterion of the system applicable to nationals of that latter State."[44]

The above-mentioned understanding of the EU citizenship beyond domestic borders entitles the Court to make an assessment to what extent the national measure at issue may "restrict the genuine enjoyment of the substance of rights of EU citizen." In other words, the Court wonders whether such domestic measure may jeopardize the enjoyment of a "European way of life," meaning the attachment of the individual to a community of values and ideals promoted by the EU. What is the meaning of "genuine substance of rights"? Azoulai resorts to the image of the "good citizen" illustrated in the Ruiz Zambrano judgment. Mr. Zambrano and his wife made clear efforts to integrate into Belgian society, their children were in school and they paid their taxes. "Such behavior is that of a 'good citizen' for whom public policy is in no way a constraint on the individual, but rather a source of 'enjoyment'. Accordingly, deportation from the Europe would amount to a real 'expatriation.' It would mean displacing an individual and its family from a place they came to occupy and which was assigned to them, a place which they were somehow 'destined' to live in" (Azoulai 2014, 13). To assess whether the genuine enjoyment of EU rights is threatened by domestic norms, the Court searches for a bond between the individual with the community, i.e. "objective traces of social integration" (Azoulai 2014, 13).

This idea of social integration applied to "good citizens" does not simply require an abstract adherence to the values of the Union laid down

[42] Case C-148/02, Garcia Abello, ECLI:EU:C:2003:539.

[43] Garcia Abello, para. 40.

[44] Garcia Abello, para. 42.

in Article 2 TEU (dignity, equality, rule of law, fundamental rights, etc.). It is the author's understanding that social integration requires that the individual is a full-fledged member of the welfare state of the host Member States. Welfare states, as created in Europe after the Second World War, aim to protect the well-being of their citizens, especially those in financial or social needs, by means of grants, pensions, and other social benefits. To accomplish this protective task assigned to the welfare state, the collection of taxes become essential to redistribute and achieve the well-being of all individuals (Hulten 2019, 33; Heins, Deeming 2015). By paying his taxes to the Belgium State, Mr. Zambrano actually contributed to the welfare state, and therefore he was socially integrated. The "European way of life" – in contrast with the "American way of life" – undoubtedly resorts to the need to achieve the well-being of the individuals through the means of the welfare state.

Until now, only in extreme circumstances such in Ruiz-Zambrano, wherein the children as EU citizens were compelled to leave the territory of the Union, the Court turned down the domestic measure. The third country national's intention to live in Europe or the simple aspiration to keep the family together in Dereci[45] is not enough for the Court to activate the protection under EU citizenship. Likewise, in the other cases (i.e. McCarthy,[46] Alokpa[47]), in which the EU citizen was not economically active and there were no risks of expulsion from the EU, the Court has been more cautious in its assessment.

For example, in McCarthy, British tax authorities denied a residence permit to a Irish national, who was also a UK national living in UK, married to a Jamaican national inasmuch as Mrs. McCarthy was not "a qualified person" (essentially, a worker, self-employed person or self-sufficient person) and, accordingly, that Mr. McCarthy was not the spouse of "a qualified person". Article 3 (1) of the Directive 2004/38 could not apply at the case at stake since Mrs. McCarthy never exercised her right of free movement and has always resided in a Member State of which she is a national. However, TFEU Article 21 is applied to purely internal situations in order to protect the right to move and reside freely within the territory of the Member States, as the Court ruled in Ruiz-Zambrano, and therefore, prevent any damage to the genuine enjoyment of the substance of rights of EU citizen. In the judgment, the CJEU concluded that the denial of residence permit did not affect her right to move and reside freely within the territory of the Union, since she can always move back to Ireland.[48]

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[45] CJEU, Case C-256/11, Dereci, ECLI:EU:C:2011:734, para. 68.

[46] CJEU, Case C-434/09, McCarthy, ECLI:EU:C:2011:277, para. 49–50.

[47] CJEU, Case C-86/12, Alokpa, ECLI:EU:C:2013:645.

[48] McCarthy, paras. 49–50.

In Alopka, the same CJEU rationale applied to the rejection of residence permit by the Luxembourg authorities to a Togolese national who immigrated to Luxembourg, and gave birth to twins, who were recognized by a French national and received French citizenship. Since their birth, Mrs. Alokpa could benefit of a derived right to live in France, and consequently the refusal by Luxembourg to grant her residence permit did not oblige her and her children to leave the territory of the Union.[49] The shortcoming of Alokpa could be read as disappointing by the commentators. As Ros observes, the conservative approach of the court gave precedence to the nationality of the twins (France), rather that the real link with the host State (Luxembourg) (Ros 2018, 151).

The CJEU's findings in Ruiz-Zambrano, promoting the values and ideals of the Union beyond the frontiers of the Member States, have been challenged in relation to expulsion orders of those committing criminal offences in the host Member State. In this field, a remarkably evolution in the case law has taken place in the direction of embracing a European society of common values. In initial cases PI and MG,[50] the Court stressed that crimes reveal the non-compliance by the person with the values expressed by the society of the host Member State in its criminal law. In such cases of "bad citizens", Azoulai noticed that the Court looked to the value system of the host Member State and therefore facilitated expelling Union citizens who breaches its domestic social cohesion (Azoula 2014, 16). Although the Court employs the formula that such behavior shows a "lack of feeling of Union Citizenship,"[51] there is no reference in the judgment to the common values of the Union's public order, which apply to the whole territory of the Union.

However in recent case law – B & Vomero, K & HF [52] – the Court has progressively engaged into promoting the values of the Union to protect EU citizens against expulsion orders (Benlolo Carabot 2019; Coutts 2018). In B & Vomero, in measuring the integrative links of the citizen with the host Member State, not only the period of imprisonment counts, but also the reintegration into European society: "the social reintegration of the Union citizen in the State in which he has become genuinely integrated is not only in his interest but also in that of the European Union in general."[53] In K & HF, the Court dealt with expulsion orders of individuals who participated in serious war crimes and remained

[49] Alopka, para. 34.

[50] CJEU, Case C-348/09, PI, ECLI:EU:C:2012:300; CJEU, Case C-400/12, MG, ECLI:EU:C:2014:9.

[51] CJEU, Case C-378/12, Onuekwere, ECLI:EU:C:2014:13, para. 24.

[52] CJEU, Joined Cases C-316/16 & C-424/16, B & Vomero, ECLI:EU:C:2018:256; CJEU, Joined Cases C-331/16 & C-366/16, K & HF, ECLI:EU:C:2018:296.

[53] B & Vomero, para. 75.

in the host Member State (Netherlands) without a legal residence permit but enjoying a family life. Although criminal offences must be assessed in light of the fundamental interests of the host Member State, protected by its criminal code, the Court underlined that war crimes "seriously undermine both fundamental values such as respect for human dignity and human rights, on which, as stated in Article 2 TEU, the European Union is founded, and the peace which it is the Union's aim to promote, under Article 3 TEU."[54]

To sum up, Ruiz-Zambrano and the latest cases regarding criminal offences identify first the territory of the Union as a space to promote certain EU values and ideals beyond the domestic borders of the Member States, and second, citizenship as a driver of social integration. The "good citizens" who pay their taxes and contribute to their welfare state of their host countries cannot be deprived from "the genuine enjoyment of the substance of rights of EU citizens." In other words, the European way of life is anchored in sharing certain fundamental values (Article 2 TEU) and the fact that the State has to provide the well-being of the individuals through the redistributive mechanisms displayed by the welfare state. Such a powerful narrative unfortunately does not apply to economic inactive citizens (i.e. Alopka, McCarthy) who do not contribute to the domestic welfare state of the host country, and therefore are excluded from the benefits derived from being members of "Territory of the Union".

4. TAXING EUROPEAN CITIZENS TO ENFORCE THE EU SOLIDARITY PRINCIPLE

The current deep EU crisis, triggered by austerity measures, migration crisis, anti-European movements in Eastern Europe and Brexit, clearly shows the lack of a feeling of membership of the "peoples of Europe"[55] to the EU polity. In other words, individuals no longer feel as members of the EU polity (Bouza Garcia 2017). The divorce between the "peoples of Europe" and Brussels is quite visible in the low turnout in the European elections. Hence, the EU integration project is doomed to fail in the short term if this feeling of "belonging" is not restored soon. The other way around, as Barroso observed, the peace narrative – the Union has been a space without wars from more than 50 years – is no longer convincing for the "peoples of Europe", and hence, a new narrative based on solidarity and social cohesion must emerge (Barroso 2013).

[54] K & HF, para. 46.

[55] It should be noted that the recipients of the EU treaties are not only the Member States but also the peoples of Europe (CJEU, Case 26/62, Van Gend en Loos, ECLI:EU:C:1963:1).

In practical terms, what does "membership" to the EU mean? How do we build up a new narrative, in Barroso's words? How can we reinforce the feeling of membership? In the author's view, two current deficits must be resolved. On one side, it means solving the so-called democratic deficit of the EU (Weiler 1997; Schimitter 2000; Heritier 1999), and on the other enforcing solidarity at the EU level.[56] Both channels undoubtedly lead to the concept of EU citizenship. In short, EU citizens, as members of the EU polity, would be citizens who democratically participate in the EU polity and pay taxes to the EU polity. The collection of such an EU tax would be redistributed among the "peoples of Europe" in accordance with the solidarity principle. Such an EU tax would aim to protect those economically inactive citizens, who are completely excluded from the benefits of the European way of life. One may wonder on which economic source of income such the EU tax would be levied. However, rather that linking taxes to a specific economic activity, wealth possession or specific purpose of the taxpayer, the modern constitutionalist doctrine boils down taxes to a mere expropriation. "After all, a tax is a form of expropriation without compensation, where not even the public purpose for which the tax was collected need be given" (Sajo 1999, 159; Menendez 2001, 121). But of course, a legitimate expropriation since it has been agreed on a democratic basis by parliament (De Crouy-Chanel 2006). Taxes aim to prevent inequality in society and therefore comply with a redistribution purpose,[57] thereby enforcing solidarity.

Malcolm Ross conceives solidarity as a constitutional paradigm in the EU, which aims to transform the EU polity, under the auspices of social justice (Ros 2010). In Ross's perspective (Ros 2010, 42), solidarity as a transformative legal concept emerges across the treaties (i.e. TEU Article 2) and specifically in the case law of the CJEU in dealing with the cumbersome relationships between social and market values (e.g. Viking[58]). However, the last financial crisis has demonstrated the failure

[56] Solidarity is not only a founding value of the EU, in articles 2 and 3 of the TEU, but also a goal enshrined in the 1950 Schuman Declaration: "Europe will not be made all at once, or according to a single plan. It will be built through concrete achievements, which first create a de facto solidarity" (Ros 2010; De Witte 2015).

[57] The scope of the theories of distributive justice and taxation goes beyond this contribution. On a detailed account of welfarist approach, the Dworkin's equality of resources and libertarian theories of distributive justice, see for example the following recent contributions (Cappelen, Tungodden 2018; Duff 2017).

[58] CJEU, Case C-438/05, Viking, ECLI:EU:C:2007:772, para. 79: "Since the Community has thus not only an economic but also a social purpose, the rights under the provisions of the Treaty on the free movement of goods, persons, services and capital must be balanced against the objectives pursued by social policy, which include, as is clear from the first paragraph of Article 136 EC, inter alia, improved living and working conditions, so as to make possible their harmonisation while improvement is being maintained, proper social protection and dialogue between management and labour."

of the EU legal principle of solidarity and conversely, only "reciprocal" solidarity has been visible, "whereby the contributor shares with the recipient in anticipation of a (future) counter-contribution or fair return" (Pantazatou 2015; Nicoli 2015). The transformative EU legal concept of solidarity, coined by Malcom Ross should evolve against these inter-governmental reciprocal responses, derived from the economic crisis, and towards a proper EU redistributive framework among the "peoples of Europe", a fully-fledged fiscal Union, as proposed by Nicoli (Nicoli 2015, 44).

The disaffection of the "peoples of Europe" with the EU integration project shows that the current contributions of the Member States to the EU budget are not enough to reinforce the two deficits mentioned above, namely the demos and the lack of EU solidarity. In the author's view, levying an EU direct tax upon the EU citizens is the concrete to build a democratic and solidary EU polity.

5. CONCLUSION

Both streams of case law by the CJEU – mutual recognition and the Territory of the Union – embrace a resilient concept of EU citizenship in light of the benchmark of EU supranational citizenship developed by Strurmia in Section 2.

However, there are serious drawbacks to achieving a proper solidarity among the "peoples of Europe" put forward in cases in the area of mutual recognition (Dano, Vatsouras & Koupatanize*)*. In these cases, the citizens cannot claim any social assistance due to scarce links with the host EU Member States. The doctrine of a "real link" with the host country jeopardizes the achievement of a truly supranational solidarity. Therein lies the precise criticisms of authors such as Ros, who argues that: "it seems that under the current change in public appetite for EU citizenship, the ECJ finds that some EU citizens are more equal than others. A perception far away from a true fundamental status for EU citizens, economically active or not" (Ros 2018, 159). A radical distinction emerges between economic active citizens who benefit from the mutual recognition principle and those who are not economically active, who are completely abandoned in the EU polity.

In the author's personal opinion, the pessimistic view conveyed by Ros must be reconciled with the other important stream of CJEU case law: the Union Territory as a space of shared values and goals, which includes solidarity. In other words, the Court is constructing a "European way of life" that reflects that the Union is not only an institutional project but also an "existential project" (Editorial Comments CMLR 2017). The

development of the EU citizenship is responsive to the emergence of the EU community beyond the States. For example, Ruiz-Zambrano, Garcia Abello, B & Vomero, K & HF look for integrative bonds of the individual the Union, beyond the borders of the host Member State. EU law becomes a tool for social integration (Azoulai 2018). The Union is not only an space of mobility of individuals under the right to free movement, but also a community that shares values and rights, consumes products or experiences culture from other Member States at home, has relatives in another European country, learns European languages, interacts with Europeans, vindicates consumer or worker rights derived from EU legislation (Editorial Comments CMLR 2017, 358). Accordingly, De Witte refers to the emancipatory power of free movement to liberate individuals from the normative choices imposed by their state of origin, and thereby allowing them to self-realize (De Witte 2016). The Territory of the Union also serves to adhere to welfare state: those "good citizens" who pay their taxes and contribute therefore to the welfare state of the host country are also protected under the EU citizenship. However, in parallel to the cases in relation to the mutual recognition, the Alopka and McCarthy cases show that economic inactive citizens are completely excluded from the protection derived from the "European way of life".

The term "European way of life" has recently crept into de political arena, insofar as the new Ursula von der Leyen Commission has appointed Margaritis Schinas to hold one of the Commission's vice-presidency of Protecting our European way of life.[59] This author does not personally understand the European way of life in a "fascist" manner, as building a fortress. On the contrary, the "European way of life" must refer not only to a space of values such as democracy, protection of fundamental rights, but also as a space of solidarity and social justice. The only possible manner to reconcile both streams of case law is to levy a tax on EU citizens, which would be redistributed according to the premises of the EU solidarity principle. Accordingly, the economically inactive citizens could benefit also from the "European way of life".

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[59] See EU Press Release 10 September 2019, *https://europa.eu/rapid/press-release_IP-19–5542_en.htm* (last visited 26 November 2019).

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TAX INCENTIVES FOR KEEPING AND ATTRACTING HIGHLY SKILLED WORKERS: THE CASE OF SERBIA

The recent increased migration of workers has posed a brain drain problem on countries, which lose their citizens to more developed countries offering better working and living conditions. Lowering the tax burden on highly skilled individuals has been one of the most commonly used incentives by both developed and developing countries. The Government of the Republic of Serbia has proposed several tax incentives for providing a more beneficial tax treatment for highly skilled employees with the aim of keeping and attracting them back. The first part of this paper illustrates the problem of emigration, the effects of emigration of highly skilled workers, and the effects of taxation on migration decisions. In the second part, the problem of brain drain and its breadth in the Republic of Serbia is addressed, and a detailed elaboration of newly proposed tax incentives is provided. Furthermore, the author proposes an additional tax incentive.

Key words: *Brain drain. – Highly skilled workers. – Migration. – Tax incentive. – The Republic of Serbia.*

1. MIGRATION

Migration of people is not a phenomenon inherent to the 21st century. People were emigrating from their home countries in pursuit of a better life from the ancient times. However, the breadth of migration has increased in the past few decades due to the demographic and economic imbalances between countries (OECD 2018, 9). Imbalances have been

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broadened further with the development of technology and its unequal dispersion across countries, especially when developed and developing countries are compared. Furthermore, the development of technology and science has reduced the costs of migration. Reduction of transportation and living costs has facilitated the migration of the increasing number of people. Moreover, advancement of technologies has provided methods for staying in contact with family members who remain in the source country while not feeling left out and homesick (OECD 2011, 125). As a consequence, there are more people migrating in search of a better life today than there were before.

Especially prone to migration are highly skilled workers: workers with a tertiary education or a specialised skill set. They are more likely to migrate to a country that offers better living and working conditions than settling in the country in which they were born (OECD 2019, 1; Fink, Miguelez 2017, 10). Better economic, working, development and living conditions are mentioned as the most common reasons for migration (OECD 2011, 125).

Increased migration of highly skilled persons is compatible with the rising demand for highly skilled labour. Countries are in need of workers who would induce the development and growth of their economies, given the much more pronounced lack of a satisfying domestic labour supply. As suggested by Liebig, Sousa-Poza (2005, 7), the growing international division of labour and technological progress nowadays requires an increased number of highly skilled individuals internationally. Highly skilled workers are needed to fill in the managerial, professional, and highly technologized job vacancies (Keery 2017, 65; Romer 2000, 222). By offering better financial conditions, developed countries are encouraged and successful in attracting highly skilled workers from outside their borders, while at the same time keeping their own highly skilled workers. As suggested by Brauner (2015, 4), since the wage gap between countries is not closing, further migrations can be expected.

The home grown labour supply has not been able to meet demand since the 1970s. It was estimated that during the 1990s, 2.5 million highly skilled workers residing in the United States of America were immigrants (Docquier, Rapoport 2009, 248). After the 2008 financial crisis, at the level of the European Union (EU), it was recognised that providing better conditions for growth requires promoting a forward-looking and comprehensive labour migration policy that would respond to the needs of labour markets (European Commission 2010, 17). Consequently, the work permit for highly skilled non-EU citizens was introduced in the EU in 2009, called the EU Blue Card, with the aim of easing the conditions and process of hiring highly skilled workers from the non-EU countries. Germany, for example, more recently introduced a new law that further

relaxes the conditions for hiring highly skilled workers from non-EU countries (for more see Taube 2018).

The need to look for highly skilled labour force outside their own borders is also caused by the fact that today's society is an ageing society (Cerna 2018). An ageing population poses the problem to productivity and growth of economies as there are not enough domestic workers to maintain and spur economic growth.

Labour shortage requires attracting foreign highly skilled workers, but it has also highlighted the need for attracting and retaining students who have migrated for study purposes (Burmann *et al*., 2018, 50; Cerna 2018, 3). Students are future workers, i.e. the pillars of economic growth, making them indispensable for countries. As suggested by Hawthorne (2018, 7–8), they provide a productivity premium to destination countries as they are far younger and with professional carriers likely to span decades, providing fiscal benefits for destination countries for a significant period. Consequently, it does not come as a surprise that the number of countries are offering better conditions for finding a job upon the completion of studies, as well as getting a work permit.[1]

Competition between countries in attracting and retaining human capital has emerged as a consequence of policies for attracting highly skilled workers and students (LaRaine Ingram 2016, 225; Brauner 2015, 20; Fink, Miguelez 2017, 2; Docquier, Rapoport 2009, 247). Countries are offering a number of incentives that aim to provide the best economic conditions, infrastructure, scientific institutions and the overall better quality of life for highly skilled workers. Competition is especially burdensome for developing countries as they have to compete with developed countries that are equipped with more and better resources (Liebig, Sousa-Poza 2005, 7). However, understanding the importance of highly skilled individuals, developing countries have started pushing back and providing incentives for keeping their highly skilled workers and students, and even attracting foreign highly skilled workers.

1.1. The Effects of Emigration of Highly Skilled Workers

The most common reason for emigration is a higher salary, i.e. better financial conditions offered in the destination country (Fink, Miguelez 2017, 11). Other reasons such as better working conditions, more and better scientific institutes, more funding for research and development activities, also influence the decision of a highly skilled individual to migrate (Burmann *et al*., 2018, 42). These are not the only reasons, but they are among the most common ones. Political stability,

[1] Countries like the United States of America, Canada, Australia, New Zealand, the United Kingdom, Germany, France, Italy, the Netherlands, Sweden and many more.

less corruption, better infrastructure, better education institutions, and many other conditions can influence the decision of workers and students to migrate.

The decision to migrate affects two countries: the source country, where the individual was born and educated before deciding to migrate, and the destination country, the country to which the individual moved with the purpose of working and living there. So, while one side loses one highly skilled individual, the other side gains. However, as we will see, the loss for the country of origin can be especially grave as it loses the treasured input for its development which is difficult to compensate.

The positive effect of immigration of highly skilled workers for destination countries has been proven. The studies showed that highly educated immigrants have a positive impact on the growth of innovation in the destination country (Bosetti, Cataneo, Verdolini 2015, 321), especially in highly technologized sectors (Fassio, Montobbio, Venturini 2019, 717). Providing positive effects on innovation, which is an essential part for the growth of the entire economy, immigrants provide the so-called *brain gain* for destination countries (LaRaine Ingram 2016, 225). In addition to inducing innovation growth, brain gain also takes the form of the free increase in the human capital stock and a fiscal gain through taxation of immigrants' income.

However, a different story can be told of the effects of the emigration of the highly skilled workers for the source country. The loss of highly skilled individuals, also known as *brain drain,* is most commonly defined as a migration of highly educated individuals towards countries offering better opportunities to the detriment of the countries of origin, particularly developing ones (OECD 2017a, 198). As suggested by the definition itself, brain drain has a negative effect on the prospects of the source country. Namely, emigration of highly skilled workers slows down the innovation and development of the source country, as there are not enough individuals who can generate development (OECD 2017a, 196–197).

The loss for the source countries can include financial and social loss, as well as a loss in human capital (OECD 2017a, 196). While the source countries have invested in the education of highly educated individuals, incurring costs for their education, after their emigration, such investment becomes a failed investment and a fiscal loss for the source country (OECD 2011, 134). The source country loses the chance to recoup the investment through the taxation of the future income of highly skilled individuals. The loss is always high, if we take into consideration that a tertiary educated individual is more likely to earn higher income compared to other workers, which even with a proportional taxation of personal income, presents a significant loss for the source country.

Developing countries are in danger of an even greater loss, as they lose the necessary human capital to spur the much needed economic growth (Arslan *et al.*, 2014, 4). The lack of highly educated individuals that could perform R&D activities, which are *sine qua non* for innovation and growth of countries, can become detrimental to the development of a developing country (Docquier, Rapoport 2009, 248). The shortage of highly skilled individuals is felt especially negatively in the sectors linked with the wellbeing, such as in the medical field (OECD 2017a, 199). Furthermore, it is argued that brain drain can lead to a reduction of investments in education by governments due to the negative return on the education investments, which can further slowdown the development of a developing country (OECD 2017a, 199–200).

On the other side, there are some arguments in literature about the positive effects of emigration of highly skilled workers for the source country. The most common argument is that emigrants, in most cases, send remittances to their families in the source country which presents an influx of foreign capital (OECD 2017a, 186; Docquiert, Rapoport 2009). It is argued that remittances present a significant source of capital for developing countries, which would not have been obtained otherwise. In order to maximise the benefit from remittances, it is argued that their tax burden in the source country should be reduced (OECD 2017a, 202–203).[2]

Data gathered on the use and effect of remittances is not very comprehensive. According to existing data, the biggest part of remittances is used for everyday consumption, providing a positive effect on reducing poverty in the country of origin (OECD 2017a, 187; Kostić 2019a, 30). However, the data on the impact of remittances on investment and growth of the economy is unclear. While the positive effects on the economic growth of countries have been advocated for, there is no data that would support it. Available data shows that only a percentage of remittances is used for acquiring land or properties (OECD 2017a, 187) which can be perceived as investing the money acquired from remittances for capital investments. However, there is no data to support the claim that remittances are used for starting a business, an investment that would have a much more significant effect on economic growth. For these reasons, it does not seem that remittances compensate for the loss that the source a country incurs after the emigration of highly skilled workers, so that the net effect for the source country might be, at least, neutral.

Consequently, for a developing country wishing to foster development and growth, it is necessary to introduce adequate policies that will enable it to retain its own highly skilled individuals. However,

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[2] For a different view on the taxation of remittances, which calls for increasing their tax burden, see especially Kostić (2019a, 30–39).

such a policy would have to base on an interdisciplinary approach, given the need to address many issues that encourage highly skilled individuals to emigrate.

1.2. Effects of Taxation on Migration

Providing better financial conditions, such as higher wages is one of the many incentives that could be used in incentivising highly skilled individuals to stay or return to the source country. Lowering tax burden and providing an individual with increased disposable net income can be seen as instrumental in providing better living and working conditions. A lower tax burden can attract highly skilled individuals with the promise of better quality of life. Concurrently, high tax burden can be seen as a disincentive for the highly skilled to migrate. In that regard, tax incentives can be seen as helpful – although not decisive – for fighting brain drain. Reducing the tax burden for the highly skilled, leaving them better off, can be a step in the right direction when it comes to their decision not to emigrate.

The effects of taxation on migration have been studied in literature, mostly concerning the question of the impact of taxes on a decision to migrate (see especially Wilson 2009; Liebig, Sousa-Poza 2005; Egger, Radulescu 2009; Halkyard 2013; Kleven *et al*. 2013; OECD 2017b). Literature suggests that taxation does play a role for migration of workers in a way that lower tax burden attracts more immigrants, especially the highly skilled ones (see especially Liebig, Sousa-Poza for intrastate migration).

According to the findings of Egger, Radulescu (2009, 1377), the progressivity of a tax system on high income brackets has the biggest impact on the decision to migrate, followed by the overall burden of personal income tax borne by an employee. Highly skilled emigrants are concerned with the net amount of their salaries, the amount that would remain for consumption after all taxes and contributions have been paid. If the net amount is not increased in the destination country, the incentive to emigrate is lowered.

As a result, the volume of tax incentives offered by both developed and developing countries for attracting foreign highly skilled workers does not come as a surprise (Burmann *et al*., 2018; 42, Halkyard 2013, 23). The consequence is the war for talent as countries have to compete in offering better conditions if they wish to attract and retain highly skilled individuals. A long list of countries, such as Australia, China, Belgium, Denmark, Finland, Italy, Israel, the Netherlands, Poland, Portugal, Spain, Sweden, the United Kingdom and New Zealand offer tax incentives that are similar in nature. The most common tax incentives are

the tax exemption for foreign source income, a reduction in personal income tax and additional incentives for employee in R&D (CESifo 2012, 70).

However, most of the tax incentives that are offered are limited in time due to their revenue cost. In Denmark, the tax scheme for attracting highly skilled individuals had a positive effect on the number of highly skilled immigrants (see especially Kleven *et al*. 2013), but only in the short term. The scheme did not motivate immigrants to stay in Denmark in the long term. However, Halkyard (2013, 30–31) advocates for the use of tax incentives even if only short term positive effects are available, due to the sharing of knowledge and the more fluid social and economic environment that is created with the migration of highly skilled workers. This fact provides an additional argument for the use of tax incentives, but not diminishing the importance of creating other positive changes in a country.

2. FIGHTING BRAIN DRAIN IN SERBIA

2.1. Emigration from Serbia in Numbers

The Republic of Serbia is an emigration country (the Government of the Republic of Serbia 2017, 26). There are more people emigrating from the Republic of Serbia, than the ones immigrating to it, especially highly skilled individuals. The vast number of highly skilled workers and students, either after graduating or leaving for studies abroad, decide to leave Serbia in search of a better life. This has been confirmed by the study performed by Gallup (2017), in which it was calculated that Serbia ranks 30th among 152 countries according to the potential net migration index.[3] Namely, the study looked at the number of people who would have emigrated had they been able to do so. According to the statistics, 27% of highly skilled workers and 46% of young people (between 15 and 29 years old) would have emigrated from Serbia had they had a chance.

Existence of a brain drain problem in Serbia has also been acknowledged by the European Commission in the Serbia 2019 Report, which states that brain drain remains an economic challenge for Serbia (European Commission 2019, 48). Even though the problem of emigration of highly skilled Serbian citizens to other countries is perceived as a problem in Serbia, there are no official national statistics that would provide precise data on the extent of the emigration. Institutions such as the Organisation for Economic Cooperation and Development (OECD), and Eurostat, the EU Statistical Office, provide some information about

[3] For more information see Gallup 2017.

emigration from Serbia in their reports and analyses of international migration.

According to the statistics provided by the OECD (2015, 41) for the period 2000–2010, Serbia was among the countries with the highest increase in the emigration rate, for both the total number of emigrants (third place out of the top 15 countries) and for the number of highly skilled emigrants (fifth place, with only one European country, Moldova, having a higher rate). According to the more recent statistics, Albania and North Macedonia are among the European countries that have a higher percentage of emigrants than Serbia.[4] The most recent data, provided by Eurostat, shows that 4,000 people per month emigrated from Serbia in 2018 and 2019, adding up to 51,000 people annually, and highlighting the extent of the emigration from Serbia.[5]

Even though it does not represent a comprehensive study on the topic of emigration from Serbia, important information has been provided in the study Migration of Students, carried out by the two ministries in the Republic of Serbia (Cabinet of the Minister in Charge for Demography and Population Policy and the Ministry of Education, Science and Technological Development). In the study, 11,013 students in Serbia were interviewed on the subject of emigration. According to the findings, around 31% of all students interviewed plan on leaving Serbia after graduating (Migration of Students 2018, 24), with 50,6% of them not planning to return to Serbia (Migration of Students 2018, 46). The main reasons for emigration are of economic nature, and they concern the prospects of finding a job in the industry for which the students qualified, low salaries in Serbia for jobs for which they qualified and a general low standard of living (Migration of Students 2018, 42). The information that supports the findings of the Gallup study is that 90% of the students that want to emigrate have the full support of their parents (Migration of Students 2018, 41). A negative finding is that only 4.3% of students would change their decision to leave if an adequate loan or other financial help was provided. The main destination countries for emigration are Germany (24%), the United States of America (11.2%), Switzerland (10.7%) and Austria (8.7%).

The data obtained in the study shines some light for the prosperity of Serbia. According to the answers provided by the interviewed students, 51.6% of them would not emigrate if a job for which they qualified were available (Migration of Students 2018, 47). A number of them highlighted the need for better scientific institutes, more respect for every occupation, less corruption, better quality of life and hiring on the basis of merit and

[4] Gallup 2017.

[5] More information available at: *https://ec.europa.eu/eurostat/data/database* (last visited 20 September 2019).

not on the basis of political affiliation. These results show that there is space for improving the conditions for living and working in Serbia. However, it shows that the changes and the effort must involve all of society, including the government, different institutions, the private sector and citizens.

Another reason for working on providing better conditions can be found in the cost that highly educated people pose when they emigrate after finishing their studies in Serbia. Important information is provided in the study The Costs of Youth Emigration, carried out by the Institute for Development and Innovations, in cooperation with the Westminster Foundation for Democracy, in 2019. The study notes that it is estimated that during the 2012–2016 period, around 245,000 people emigrated from Serbia. Especially important findings of the study are the findings on the costs for the Republic of Serbia of each highly educated individual who emigrates. It is calculated that the cost for the budget of the Republic of Serbia of one highly educated person who emigrates amounts to around EUR 34,000, while the cost is increased up to around EUR 55,000 for each PhD student (Institute for Development and Innovations 2019, 21). Moreover, it is calculated that the aggregate cost of emigration of highly educated people for the budget of the Republic of Serbia is somewhere between EUR 960 million and 1.2 billion (Institute for Development and Innovations 2019, 23).

2.2. Proposed Tax Incentives

Targeting the right problems and providing adequate solutions is the path that the Government should follow. The results provided by the mentioned studies on emigration from Serbia could prove to be very helpful for the Government when designing incentives for retaining highly skilled individuals and attracting the return of the ones already abroad.

Tax incentives, as mentioned above, can have an impact on the decision to emigrate. Given that developed countries are offering tax incentives for highly skilled workers so as to attract them, the Republic of Serbia has started the work on introducing tax incentives that can help them decide to stay or to come back to Serbia.

In 2018 the Republic of Serbia introduced an entire set of tax incentives for the knowledge based economy which should help boost the growth of innovation in the Republic of Serbia. These incentives can be expected, at least indirectly, to provide better working and living conditions in Serbia through incentivising business development in Serbia. Tax incentives such as a double recognition of R&D costs, with salaries for individuals performing R&D activities benefiting from the

incentive, is expected to have a positive effect on the desirability of hiring highly educated individuals, and consequently on the increase in income of those individuals. Furthermore, an incentive for investing in newly established innovative companies (start-ups) is provided, as well as the more beneficial tax treatment of employee stock options plan. Another incentive offered is the IP Box which reduces the corporate income tax rate to about 3%, compared to the regular 15%, for income acquired from licensing of intellectual property rights that were developed in the Republic of Serbia.

Given the large number of people who emigrated from developing countries, attracting them to return is of great importance for the country of origin due to the fact that they bring back the financial, social and human capital (OECD 2017a, 192). One of the most important aspects of the financial capital that is brought back is the way that businesses are started upon return and investment in entrepreneurship. According to the studies, returning emigrants are more prone to starting their own businesses upon return (OECD 2017a, 193). For this reason, it can be expected that the newly introduced incentives for knowledge based economy will have at least an indirect effect on the desirability of living and working in Serbia which would also help economic growth.

The return of highly skilled workers can also have a positive effect for the source country through the sharing of knowledge and consequent development. After the return, repatriates can lead to an increase in the human capital stock in the source country due to the sharing of knowledge and skills that they are bringing back (OECD 2017a, 194). For that reason, an additional incentive has been proposed in this paper which aims to ease the conditions for investing in the skills and education of future employees by legal entities in order to support the growth of human capital in Serbia.

Acknowledging the importance of returning emigrants, as well as of attracting highly skilled individuals from other countries, the Government of the Republic of Serbia has proposed the introduction of a set of tax incentives by the end of the 2019, aimed at relaxing the financial conditions for returning highly skilled emigrants and reducing costs of hiring new employees.

2.2.1. Deduction of 70% of Salary Tax for New Residents

One of the proposed tax incentives is directed at providing a better financial position for the highly skilled workers returning or moving to Serbia. Moving to another country involves costs that have to be borne by the emigrant. In order to facilitate the process of moving, countries have started offering incentives that aim to reduce the moving costs or lowering the costs of living and working in the destination country.

Incentive proposed by the Government of the Republic of Serbia follows the logic of the '30% ruling' adopted in the Netherlands. Incentive offered in the Netherlands allows up to 30% reduction of the tax base for salary tax purposes as compensation for moving costs to the Netherlands. To benefit from the incentive, the taxpayer has to have been living outside of the Netherlands for no less than 16 months before starting to work in the country, and to possess specific expertise that is not available or only scarcely available in the Netherlands. Whether the specific expertise condition is fulfilled is proven by a minimum salary that repatriates must earn in the Netherlands, while such a limitation does not exist for individuals performing scientific research at a designated research institution. In the Netherlands, this incentive is offered for five years.[6]

Portugal also offers beneficial tax treatment to new residents. According to the incentive, new residents performing highly qualified activities in the field of science, technology and arts in Portugal, can benefit from a flat income tax rate of 20%, instead of the regular 40%. To benefit from the lower tax rate, the individual must not have been a tax resident of Portugal for five years before moving to the country.

Another interesting tax incentive is provided in Italy for inbound repatriates and foreign highly skilled workers, with the aim of putting a stop to brain drain.[7] The incentive targets highly skilled individuals and should in turn have a positive effect on the development and progress of the country. This incentive has been offered since 2016 as a 50% reduction of taxable employment and self-employment income, while in 2017 the tax deduction was further increased, leaving only 30% of the employment income taxable.

To benefit from the Italian incentive, the highly skilled individual has to hold a degree, high qualification, specialization or to perform managing roles and to be employed or perform activities for an Italian resident company or a company related to it. Incentive is offered to highly skilled individuals from both EU member states and non-EU countries with which Italy has signed a double tax treaty or an information exchange agreement. Furthermore, the highly skilled worker must not have resided in Italy for five years before moving to the country, while planning to remain in Italy for at least two years after becoming Italian tax resident.

[6] For more information about the '30% ruling' offered in the Netherlands see at: *https://www.belastingdienst.nl/wps/wcm/connect/bldcontenten/belastingdienst/individuals/living_and_working/working_in_another_country_temporarily/you_are_coming_to_work_in_the_netherlands/30_facility_for_incoming_employees/* (last visited 23 September 2019).

[7] Law No. 232. 2016. Bilancio di previsione dello Stato per l'anno finanziario 2017 e bilancio pluriennale per il triennio 2017–2019 [State budget for the 2017 financial year and multi-year budget for the 2017–2019 three-year period]. *Gazzetta Ufficiale Serie Generale* No. 297, 21 December 2016 – *Suppl. Ordinario* No. 57.

The right to use the tax incentive is allowed for five years, starting from the year in which the highly skilled individual became the tax resident of Italy.

Taking into consideration the abovementioned incentives and their effects, the incentive proposed by the Government of the Republic of Serbia can be said to follow their logic. Incentive is offered through the reduced tax burden for highly skilled individuals that are of great significance for the development of the economy.

The proposed tax incentive requires an amendment to the Law on Personal Income Tax[8]. According to the incentive, the regular salary tax base is reduced for 70%, leaving only 30% of salary income taxable for highly qualified workers. To qualify for the deduction, the highly skilled individual has to obtain a full employment contract for an indeterminate period. The right to use the benefit is limited to five years from the day of the signing of the employment contract.

To be regarded as a highly skilled individual, the individual has to occupy a position for which a specific professional education is required and for which there is a demand that cannot be easily satisfied in the domestic labour market in Serbia. In order to avoid complex definitions that would, most likely, unintentionally preclude individuals from some occupations to benefit from the measure, the solution used in the Netherlands has been adopted. Namely, the salary obtained by the individual is used as a criterion: if the salary of an individual is higher than the three average monthly salaries per employee in Serbia (in the case referred to in paragraph a) below), or higher than the two average monthly salaries in Serbia (in the case referred to in paragraph b) below), that individual will be regarded as a highly qualified individual.

Further explanation of a highly skilled individual is provided in the provisions. In order to benefit from the incentive, the individual who moves to Serbia should fulfil one of the two requirements that: a) 24 months before the day of signing of the contract with a qualified employer, they did not mainly reside in the territory of the Republic of Serbia, or b) 12 months before the signing of the contract with a qualified employer they mainly resided outside the territory of the Republic of Serbia for reasons of further education or advanced training, and at the moment of signing of the contract with a qualified employer, they are younger than 40 years old.

[8] Zakon o porezu na dohodak građana [Law on Personal Income Tax], *Official Gazette of the RS*, 24/2001, 80/2002, 80/2002, 135/2004, 62/2006, 65/2006, 31/2009, 44/2009, 18/2010, 50/2011, 91/2011, 7/2012, 93/2012, 114/2012, 8/2013, 47/2013, 48/2013, 108/2013, 6/2014, 57/2014, 68/2014, 5/2015, 112/2015, 5/2016, 7/2017, 113/2017, 7/2018, 95/2018 and 4/2019.

As it can be noted, this incentive is open to nationals of all countries, and not just to Serbian citizens. However, individuals moving to Serbia have to be regarded as Serbian tax residents in accordance with the centre of personal and economic interest rule, and in accordance with all Serbian double tax treaties.

To benefit from the incentive, the highly skilled individual has to be employed with a qualified employer. A qualified employer is an employer who is a tax resident of the Republic of Serbia and who is not a related party to the previous employer of the highly skilled individual. Namely, the incentive is not extended to employers who are relocating employees to their related parties in Serbia, as it is assumed that they would have done so even without the incentive, should there be a reason for their relocation.

Nonetheless, there is an exception to this rule. Any employer will be regarded as a qualified employer in the case of a highly skilled individual who, in the 25 years preceding the year in which the contract is signed, has been a tax resident of the Republic of Serbia for at least three years (having a domicile or a centre of personal and economic interests in Serbia). Namely, if an employee was, in any period of their life, regarded as a tax resident of the Republic of Serbia for three years (not necessarily consecutive years), it will be possible to use the incentive even if the employer does not fulfil the abovementioned condition. The main objective of the incentive is to attract Serbian emigrants to return to Serbia, and with this exception, the incentive is open to those who once lived in Serbia, but who emigrated and worked for an employer who is regarded as a related party to the new employer in Serbia.

The issue of the relevant compulsory social security contributions regime is related to the deduction of the tax base for salary tax. In order to truly decrease the costs for employers and employees, it is proposed that the base for social security contributions be reduced by 70% for highly qualified employees. Consequently, the tax base for compulsory social security contributions would be reduced as well, and an incentive would be offered to both employees and employers through the reduction of salary tax and social security contributions.

2.2.2. Special Treatment of Capital Gains of New Residents

The second proposed incentive addresses the widespread international business practice of awarding employees with own securities for free or under preferential regime (Kostić 2019a, 54). The practice serves as a measure for uniting the interests of employers and employees which should provide a positive effect on the growth of the business. By sharing the ownership of the company with employees, employees are motivated to work harder in order to increase the value of the shares so

that they gain from it too, while the employer benefits from more loyal and productive employees.

Even though such practice is not widespread in the Republic of Serbia, by inviting highly skilled emigrants to return to Serbia, there is a need for adjusting the existing legal framework, as some of them might own securities that they do not wish to sell before moving back to Serbia. Moving to Serbia while owning the securities would make the securities subject to the capital gains tax in Serbia upon their sale, even though they were not acquired in Serbia, nor by a Serbian tax resident at the time of their acquisition.

According to Article 72 of the Law on Personal Income Tax, the taxpayer is required to a pay capital gains tax on the sale of securities that they have owned for less than 10 years. In that case, the tax base for capital gains tax is the difference between the purchase price (at the time of the acquisition) and the sale price, with a tax rate of 15% (Articles 72–77 of the Law on Personal Income Tax).

The newly proposed measure adjusts the purchase price with the aim of lowering the burden for capital gains tax for the sale of securities issued by a non-resident company that the taxpayer acquired for consideration. If, at the time of acquisition and six months following the acquisition of those securities, the taxpayer was not a tax resident of the Republic of Serbia, the purchase price will be the market price on the day when the taxpayer became the tax resident of the Republic of Serbia.

The step up in basis allows for taxation of only the part of the increased value of the capital after the taxpayer became a tax resident of the Republic of Serbia. It provides the taxpayer with a beneficial treatment as the difference between the purchase price at the time of the acquisition, and at the time of becoming a tax resident of the Republic of Serbia will be different, i.e. the price will be higher in the latter case, which would reduce the difference which is subject to the capital gains tax. As a consequence, the taxpayer will be subject to a lower tax burden, which should reduce the costs for moving to the Republic of Serbia.

2.2.3. Tax Exemption for Start-up Employees – Founders

In 2018, the Republic of Serbia introduced a set of tax incentives intended to foster the growth of the knowledge based economy. Special attention was paid to tax treatment of newly established companies that perform innovation activities, commonly known as start-ups. Start-ups are set up by a small number of individuals around an innovative business idea. However, a significant amount of capital is required to develop an innovative business idea, which represents the most common obstacle to the development of start-ups. Targeting the capital requirement, incentives were introduced for reducing the costs for start-ups and providing them

with the much needed capital. These incentives introduced the tax credit for investments in start-up capital, a double deduction of R&D costs and a reduced tax burden for royalties.

The Government has proposed an additional incentive for reducing the costs for start-ups even further. It is proposed that the tax burden for salaries of founders of a start-up is reduced. Start-ups would be exempted from paying the calculated and deducted salary tax for salary of founders which are employed in the start-up. The employee-founder has to sign an employment contract and to be registered for compulsory social security insurance. Further, the employee– founder has to own at least 5% of shares or stocks in the start-up. If there are multiple founders which are employed in the start-up, the benefit is provided for each one.

The tax exemption applies to monthly salaries up to 150,000 RSD. If the salary is higher, the tax exemption is provided only for the amount of 150,000 RSD, while the tax exemption does not apply for the remaining part of the salary. If one individual is founder of two or more start-ups, only one start-up has the right to use the benefit for that individual; the other start-ups cannot benefit from the tax exemption for the same individual.

The start-up has to be registered with the competent authority and it cannot be regarded as a related party to any legal person, in accordance with the Law on Corporate Income Tax. Also, it must not derive more than 30% of its total income from other entities that are regarded as related parties to any of its founders. The right to use the benefit is available for 36 months from the incorporation of the start-up, which cannot be later than the 31st December 2020.

This incentive cannot be cumulated with any other incentive available for hiring of the same individual, except for the incentives prescribed in the law governing compulsory social security insurance, even if they are prescribed as a subvention for employment or self-employment. Given that the Law on Personal Income Tax in Article 21dj already allows the tax exemption for salaries of founders of newly established companies, it was necessary to limit their mutual use. However, given that the tax exemption from Article 21dj is allowed only for salaries of employees-founders up to 37,000 RSD, and only for 12 months from the incorporation of the company, it is clear that the newly proposed incentive will be of greater benefit to start-ups.

Contributions for social security insurance impose a higher cost on employers and employees. In order for the tax incentive to be efficient in actually reducing the overall costs, it was necessary to provide a complementary incentive for contributions for social security insurance. For that reason, the tax incentive has been transposed in the field of the compulsory social security insurance. Namely, the incentive proposes to exempt the employer from paying social security contributions, on both

employer's and employee's accounts, for salaries of founders-employees up to 150,000 RSD. If the salary is higher, the part above the limit will not benefit from the exemption. The same conditions have to be fulfilled as for the salary tax incentive. While benefiting from the incentive, contributions for the compulsory social security for founders-employees will be payable from the budget of the Republic of Serbia for the lowest monthly base for contributions.

2.2.4. Tax Exemption for Salaries of New Employees

The proposed tax incentive for individuals moving to Serbia, which provides a 70% salary tax deduction, is open solely to taxpayers who are new tax residents of the Republic of Serbia or repatriates. Namely, current tax residents of the Republic of Serbia are excluded from the scope of that incentive. While not diminishing the value of attracting emigrants to return to Serbia, in order to provide overall better working and living conditions in Serbia, so that other individuals do not emigrate, an additional tax incentive is proposed.

Tax incentive introduces a beneficial tax treatment of salaries for newly employed individuals, mainly targeting younger citizens[9] and individuals who were working, i.e. performing services, as entrepreneurs. An increasing number of entrepreneurs was noticed in Serbia, with individuals registering as entrepreneurs for providing services to their contractors, as it allowed them to avoid an employment relationship and the increased accompanying costs. The situation has led to the abuse of the entrepreneurship status, i.e. to the bogus self-employment[10]. The problem with the practice is that the relationship between the entrepreneur and the contractor is practically the one between an employer and an employee. Namely, in practice, entrepreneur does not act independently from the contractor in performing activities. The contractor is the one who undertakes all the risks and who organizes the work of the 'entrepreneur', and not, as it should be, the entrepreneurs themselves.

Bogus self-employment is not a phenomenon unique for Serbia; it is present in other countries, which started introducing measures for putting an end to it. The most famous decision in the area of bogus self-employment is the decision of the Court of Appeal of the United Kingdom in which the practice of hiring Uber drivers as entrepreneurs was seen as a disguise of an employment contract between Uber and its drivers.[11]

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[9] At the moment, unemployment rate of people between 15 and 24 years old in Serbia is high, 22.4%.

[10] For more about bogus self-employment and the ways to tackle it see especially Collins, Horodnic 2017.

[11] The decision of the Court of Appeal of the United Kingdom available at: *https://www.judiciary.uk/wp-content/uploads/2018/12/uber-bv-ors-v-aslam-ors-judgment-19.12.18.pdf* (last visited 29 September 2019).

The current legislative framework in the Republic of Serbia allows individuals to register as entrepreneurs and pay less taxes and contributions than employees and their employers. For that reason, companies will gladly choose the role of a contractor rather than employer, and individuals will rather choose higher net disposable income than incurring higher costs for salary tax and accompanying contributions. Such a disproportionate status of contractors/employers and entrepreneurs/employees, pointed to the need of equalising their statuses and preventing the discrimination against employers and employees, at least for tax law purposes.

Equalising the position of employees and entrepreneurs who have abused the rules, is expected to have an additional positive impact through the increase in labour rights. New rights would become available to new employees (previously entrepreneurs), such as maternity leave, public health insurance (which is still better compared to the private health insurance which does not cover a vast number of more complex medical issues), severance pay, and other rights available to workers in an employment contract, but not to entrepreneurs.

Furthermore, providing a legal solution for bogus self-employment is expected to increase legal certainty in the tax system as well. Taxpayers would have all the necessary information to choose the legal form that best suits the activities that an individual wishes to perform. Taxpayers would know precisely when they are allowed to register as entrepreneurs and when they fall under the normal employee rules, as well as the tax consequences of both statuses.

For the mentioned reasons, a measure has been proposed by the Government which 'tests' the level of independency of registered entrepreneurs in providing services to their contractors. According to the proposed measure, if an entrepreneur 'fails' the test, their income will be regarded as 'other income' for the purposes of the Law on Personal Income Tax which induces an increased tax burden (the tax rate is 20% compared to regular 10%), as well as increased social security contributions.

Introduction of this measure would affect the disposable net income of former entrepreneurs (new employees), as well as the cost for their former contractors, i.e. new employers. In order to provide a transitional solution that would enable entrepreneurs and their contractors to get used to the new circumstances and the new test, the Government has proposed a measure that reduces their (increased) costs during a medium term period of three years.

The new tax incentive provides a tax exemption for employers from paying (in a certain percentage) the calculated and deducted salary tax for qualified individuals. The tax exemption is granted for 36 months,

and exempted percentages depend on the year in which the salary is payable. For the year of 2020, the amount is 70% of calculated and deducted tax, for 2021 that is 65%, and for 2022 it is 60%. By providing this type of incentive, employers are indirectly granted a subvention that would neutralise the latest increased costs.

The incentive is open only for employers who hire qualified individuals. A qualified individual is defined as a newly employed individual who was not registered as an insured employee during the period from 1 January to 31 December 2019, but which gained the status of a registered employee of the qualifying employer or any other employer during the period from 1 January to 30 April 2020. Namely, entrepreneurs were not registered as employees for the purposes of social insurance while providing services as entrepreneurs, which makes this measure available to them, as well as to other individuals who have found their first job.

The right to use the incentive is available to qualifying employers, which are defined as any an employer, legal or physical person, which during the period from 1 January 2020 to 31 December 2022 signs an employment contract with a qualified individual and registers the employee for compulsory social security contributions with the competent authority. Furthermore, the employer has the right to use the incentive if it increases the total number of employees after hiring a qualifying employee, compared to the number of employees on 31 December 2019. The right to use the benefit is also available to any employer which starts to conduct business activities after the 31 December 2019.

If the employer, while using the incentive, decreases the number of employees compared to the number it had on 31 December 2019 (increased for the number of qualified employees), the employer loses the right to use the incentive for an equivalent number of qualified employees. In the case of an employer who started performing business activities after 31 December 2019, the relevant date is 31 December of the year in which it started performing business activities.

This incentive cannot be cumulated with any other incentive offered for hiring individuals, except from the one offered in the law governing compulsory social security contributions, nor can it be used by public authorities.

In order to reduce the overall employment costs, and not just the salary tax, exemption from paying contributions for pension and disability insurance of qualified employees has been provided to employers. Exemption is provided to both employer's and employee's accounts, but only for pension and disability insurance contributions. Given that pension and disability insurance contributions amount to 70% of total social

security contributions, it can be argued that an important reduction has been provided. Additional reduction in contributions for health insurance is avoided as it would have had a negative effect, given that the reduced revenue of the Republic Fund for Health Insurance would have had to be compensated from the budget of the Republic of Serbia, which does not happen normally, unlike the case of pension insurance.

To benefit from the incentive, the same conditions as for the incentive regarding the salary tax must be fulfilled, while the exempted percentages differ. For salaries paid in the year of 2020, 100% of contributions for pension and disability insurance are exempted, for 2021 the figure is 95%, and for 2022 it is 85%. In that period, contributions for compulsory pension and disability insurance for employees are payable from the budget of the Republic of Serbia. This incentive cannot be cumulated with any other incentive (except the complementary incentive for salary tax) intended for hiring the same individuals.

2.2.5. Tax Exemption for Foreign Source Income of Non-residents

Rapid technological advancement has changed the way of doing business and performing services. The need to be in one place physically to perform work tasks does not stand in many cases. The Internet has enabled individuals to work from anywhere in the world using their personal computers, which has posed problems for controlling and taxing the income of those individuals.[12]

Serbia is one of the countries that find it difficult to track the income of persons performing activities while temporarily staying in Serbia, leading to non-taxation even though the right to tax exists. For that reason, it is seen as a good practice to formally exempt the income received by a non-resident individual from abroad, while temporarily staying in the territory of the Republic of Serbia. This measure would equalise the legal framework with the reality and increase tax certainty. Furthermore, it is believed that this measure would provide an incentive for foreign individuals to come and work in Serbia temporarily. Even though they would not pay income taxes, the benefit for the Republic of Serbia would be provided through the increased VAT revenue from their consumption in Serbia.

The proposed incentive introduces exemption from personal income tax for income obtained by a non-resident individual who spends a maximum of 90 days in the Republic of Serbia, in the period of 12 months starting or ending in the respective tax year. To benefit from the exemption, the work has to be performed for a non-resident contractor who does not perform main business activities or other activities in the Republic of Serbia.

[12] For more see: Kostić 2019b.

If the non-resident contractor performs activities in the Republic of Serbia, the income of a non-resident individual will be exempted if the service performed is not used for contractor's main business activity or other activity that it performs in the territory of the Republic of Serbia. Introducing the limitation that the non-resident principal does not perform business activity in the Republic of Serbia aims to safeguard the equal position of resident and non-resident entities by reducing potential for discrimination.

2.3. Proposal of an Additional Tax Incentive: Tax Incentive for Investing in Training and Education of Future Employees

An additional tax incentive is proposed in this paper, with the aim of supporting highly skilled persons remaining in the Republic of Serbia and attracting those who have left.

The incentives proposed by the Government (explained above) aim to reduce costs for employers and indirectly providing more disposable net income to employees. Having in mind that economic conditions are not the only one affecting the decision to emigrate, it is necessary to build an environment where the further development of skills and lifelong learning are encouraged. Employers should be encouraged to invest in further specialisation and education of their employees and future employees as it would provide them with more skilled workers. Employees and future employees, on the other hand, would benefit from the personal development, which would enable them to advance their careers, earn higher income and secure higher quality of life in Serbia, which would reduce the brain drain from the Republic of Serbia.

Incentives offered by employers to their employees as a way of tuition fee assistance have been proven to provide a positive return on investment. According to the study performed by the Lumina Foundation regarding the tuition fee assistance provided by a health care insurance provider to its employees in the United States of America, it was shown that the investment paid off with a 129% return to the employer, while the employees benefited from a 43% salary increase in the three following years (Lumina Foundation 2016, 9–10). Furthermore, a study by the OECD showed that government investment in skills is a sound investment, as every dollar invested is more than fully repaid by the increased future tax revenue (OECD 2017b). Having in mind these facts, there is an incentive for introducing similar measure into the legal framework of the Republic of Serbia as both employees (present and future) and employers benefit from the incentive: the former through the further specialisation and reduced salary tax, and the latter through reduced employment costs and better qualified personnel. Moreover, a gain for the Republic of Serbia would be obtained through the reduced brain drain that would allow its faster economic growth. Individuals would have a secure job in

the field for which they qualified, directly disincentivising them from emigrating.

The current legal framework of the Republic of Serbia does not recognise any specific incentive for investing in the education or specialisation of current and future employees. However, in line with the current provisions, an employer that invests in the work related education or specialisation of its current employees will be allowed to deduct the amount invested as an expenditure if the money was paid directly to the institution or organisation providing the course.[13] Furthermore, the amount invested will not fall into the tax base for salary tax of the employee who benefits from the investment. If, however, the money was paid into the account of an employee, who would pay the course cost himself from the money obtained from the employer, the employer would not have the right to deduct the amount as an expenditure, and the amount obtained would fall into the tax base as an in-kind benefit for salary tax purposes, inducing an increase in the compulsory social security contributions. As a result, only employees whose course cost has been covered directly to the institution providing the course will be able to benefit from the employer's investment in their education or specialisation.

Investment in education or specialisation of individuals who are not current employees of a legal entity, such as students, would have to incur the personal income tax (for the part exceeding the legally prescribed monthly maximum of around EUR 100) according to Article 85 of the Law on Personal Income Tax, as 'other income', with a 20% tax rate. Furthermore, it is unclear whether the legal entity would be able to deduct the invested amount as an expense. It can be argued that if a contract in which the individual commits to working for the investor after completing the course is provided, the employer would have the right to deduct the invested amount. If there is no similar contract, there would be no sufficient relationship with the business activity, and the expenditure would not be permitted. We can notice that there is no actual incentive for legal entities to support the specialisation of individuals who could become an invaluable asset for the business activity.

The situation is not much better even if a legal entity wishes to invest in entities that are registered for providing education services. In that case, legal entity has the right to deduct the sum invested as expenditure, but the maximum deductible amount is capped at 5% of investor's total revenue.[14] It is noticeable that these rules do not provide

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[13] Opinion of the Ministry of Finance of the Republic of Serbia, No. 414–00–88/2002–04.

[14] Zakon o porezu na dobit pravnih lica [Law on Corporate Income Tax], *Official Gazette of the RS*, 25/2001, 80/2002, 80/2002, 43/2003, 84/2004, 18/2010, 101/2011, 119/2012, 47/2013, 108/2013, 68/2014, 142/2014, 91/2015, 112/2015, 113/2017 and 95/2018, Art. 15.

an actual incentive for companies to engage in direct or indirect investments in human capital.

The desirability of an incentive that would further support investments in human capital in Serbia is supported by the fact that only 16% of people in Serbia have acquired tertiary education (European Commission 2019, 30). Creating a knowledge based society and economy would be impossible without persons who would drive the development. This is even more so taking into consideration the rapid advances in technology that have already changed the way of doing business and introduced new required skills (Fitzpayne, Pollack 2018, 1; York 2019). Tuitions for further studies abroad can be especially very high and unattainable for students, but significantly beneficial due to the resources and opportunities offered by studying the latest achievements in the relevant field. Employers are in demand of such highly skilled workers and only by supporting their development can they both prosper.

The incentive proposed in this paper would require changes to the Law on Personal Income Tax and the Law on Corporate Income Tax.

It is proposed that if an employer covers the cost of a training or a course for a future employees, the total amount invested should be deductible from the employer’s corporate income tax base as an expenditure, during the period in which the investment was made. Further, the benefit provided to the future employee would be exempted from personal income tax, i.e. the other tax, and it would not give rise to social security contributions. If the employer does not have enough taxable income from which it could deduct the whole amount invested, the right to carry over the remaining part of the investment would be allowed for up to five years.

To benefit from the incentive, it is necessary that the individual signs a contract with the future employer in which they would commit to working for the legal entity that covered the course cost, for at least two years. If the individual does not sign an employment agreement with the legal entity after the completion of the course, or terminates the employment voluntarily before the two years period has expired, they will be obliged to repay the total cost to the legal entity and to pay the personal income tax, i.e. the other tax, for the whole amount obtained.

The legal entity must be a tax resident of the Republic of Serbia in order to benefit from the incentive. Furthermore, the right of the individuals to apply for funding from their employer has to be available to all individuals who satisfy the requirements posed. The legal entity will decide whether it wishes to fund the specific course according to its business needs.

The qualifying training or education courses have to be work related, i.e. in the interest of the business activity performed by the legal

entity, otherwise, the incentive will not be applicable. The training or education course has to be related to the activities that the legal entity performs as its business activity. If the course is directed at obtaining personal gain for the employee but is not related to legal entity's business needs, the costs will not be deductible (such as obtaining a driving license if the job does not require it). Costs of obtaining another professional vocation (e.g. a secretary taking a course to become an accountant) will not fall into the category of qualified courses if it is of no use to the legal entity.

Costs that can be deducted are:

- the actual course cost (course fee),
- the costs of course materials such as specialised literature,
- daily allowance, if provided by the legal entity,
- travel costs, if provided by the legal entity,
- accommodation costs, if provided by the legal entity.

The maximum amount of the costs that the legal entity can deduct in one fiscal year is not capped. Namely, the incentive provides benefits for both parties, the legal entity and the individual, but it also provides a benefit for the Republic of Serbia. More highly educated and specialised workers will lead to the increase in the number of tertiary educated and highly specialised workers in Serbia, which would help economic development.

As specifically provided in Article 2 para. 4(3) of the Bylaw[15] for applying the double deduction of R&D costs, according to Article 22g of the Law on Corporate Income Tax the costs for training of employees, and consequently of future employees, cannot be deducted in a double amount. This limitation provides a safeguard against eventual abuses of the incentive, while allowing the improvement of the current situation.

3. CONCLUSION

The importance of human capital, especially of the highly skilled individuals, has never been as important for the development of economies as it is in today's rapid technological advancements. Mobility of people, which has been constantly increasing, has speed up in the recent decades.

[15] Pravilnik o uslovima i načinu ostvarivanja prava na priznavanje troškova koji su neposredno povezani sa istraživanjem i razvojem u poreskom bilansu u dvostruko uvećanom iznosu [Bylaw on the conditions and the method for exercising the right of recognition of expenditures directly related to research and development in the tax balance sheet in a double amount], *Official Gazette of the Republic of Serbia*, 50/2019.

People, especially the highly skilled ones, are more inclined to leave their home countries, homes and families in the search of a better life. There are many reasons why individuals leave their homes, but the most common one is the need for better economic conditions.

This trend has posed problems for countries which are losing the talents that could help them grow. Such a problem is especially grave for developing countries when they have to compete with developed countries for talents. However, developing countries have realised that they need to fight back and various incentives have been offered. One type of these incentives are tax incentives, as studies have showed that taxation plays a role in the decision for emigration.

The Republic of Serbia is the talent exporting country facing the problem of brain drain. According to the available statistics, the brain drain is not reducing, which demands a response from the government, in providing better living and working conditions. For that reason, the Government is at the moment proposing a set of tax incentives for reducing the tax burden of highly skilled workers. These incentives have been drafted following existing incentives in other countries, benefiting from their experiences. The incentives that are proposed are a 70% deduction of salary tax for new residents, the step up in basis for capital gains tax for new residents, the tax exemption for salaries of employees-founders of start-ups, the tax exemption for new employees and the tax exemption for the foreign source income of non-residents.

Furthermore, this paper proposes an additional tax incentive, which is proposed in order to promote investing in the education and skills of individuals, i.e. of future employees, willing to work on their professional development. Legal entities are encouraged to invest in the education and specialisation of future employees, by allowing them to deduct the entire amount invested in the training or education of future employees. Incentive is open for courses that are related to the business activity of the legal entity covering the course cost. This incentive is meant to increase the human capital stock in the Republic of Serbia, to increase the number of tertiary educated people who could lead the development of the country.

All of these proposed tax incentives should have a positive impact on the reduction of the brain drain in the Republic of Serbia, which is posing a threat to the country’s development. Attracting and retaining highly skilled individuals, which will come at a cost in the form of reduced tax revenues in the short term, should help innovation and economy grow in the long term, through the activities of highly skilled individuals performed in the country. For that reason, steps undertaken by the Government of the Republic of Serbia can be seen as a step in the right direction for improving the country’s prospects.

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BRAIN DRAIN AND TAX COMPETITION: DO WE NEED ANOTHER BEPS?

In the article we argue that the origins of the international tax base erosion in the corporate sector, which are the harmful tax competition for capital and old-fashioned international tax rules, are also relevant for the taxation of income of the high-skilled and mobile workforce. Therefore, a multilateral rethinking of the global tax architecture is proposed in order to conceptually address the problem properly and in a harmonized manner. We point out, based on the examples of Russia and Serbia, several problems of tax base erosion for mobile "talents", with a case study analysis of scenarios of "talent" migration involving sportspersons, researchers and IT specialists. Finally, we propose some ideas for global tax cooperation in order to mitigate the negative tax effects of brain drain based on adapting the existing recommendations of the BEPS Project for the cases of migrating individuals.

Key words: *BEPS. – Brain drain. – Tax competition. – OECD Model Convention. – Tax residence.*

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1. INTRODUCTION

Imagine you are playing Who Wants to Be a Millionaire? on Italian TV. The host asks you the last question (the answer to which can set you up for the rest of your life) – "What makes Italy lose about 14 billion euros annually, which equals approximately 1% of its GDP?" (*ANSA Politics* 2019) You are given four options, but you don't know the correct answer to the question. You turn to your lifelines: Ask the Audience, 50:50, Phone a Friend. Initially, you call your old friend, but on the end of a telephone they tell you that he moved to another country for a better life. Ok, you take another lifeline, 50:50, but the host apologizes and tells you that the show editor was recently offered higher salaries in the US, and therefore, he quit. Wha-a-at! You turn to Ask the Audience, but there is no one in the studio either – everyone has chosen to leave the country. Sounds like a nightmare for any trivia player!

You probably have already realized what is the correct answer to the question. It is *brain drain*, which does not have an unambiguous definition, but rather a list of definitions:

– emigration of educated or professional people from one country, economic sector, or area for another usually for better pay or living conditions;[1]
– migration of health personnel in search of the better standard of living and quality of life, higher salaries, access to advanced technology and more stable political conditions in different places worldwide;[2]
– the situation in which large numbers of educated and very skilled people leave their own country to live and work in another one where pay and conditions are better.[3]

The modern world is characterized by a high degree of inequality in the context of the brain drain. We turn to one of the studies of the Gallup Institute (2018), in which the authors tried to determine how much the population of a give country would change if everyone willing to move to another country really moved to where they wanted (Potential Net Migration Index – PNMI). The results are quite shocking – for 109 out of 150 countries negative the values vary from –1% to –70%.

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[1] See the definition of *brain drain* in the Merriam-Webster Dictionary. *https://www.merriam-webster.com/dictionary/brain%20drain* (last visited 25 September 2019).

[2] See Megan Ivy. Why brain drain hurts a developing nation? *https://borgenproject.org/brain-drain-hurts-developing-nation/* (last visited 25 September 2019).

[3] See the meaning of *brain drain* in the Cambridge English Dictionary. *https://dictionary.cambridge.org/dictionary/english/brain-drain* (last visited 25 September 2019).

However, we presume that the impact of tax burden on the decision to leave is insignificant. In particular, the comparison of the Gallup Institute (2018) data with the national tax rates (NTR) for the jurisdictions of some leaders and outsiders, according to KPMG (2019a), may also support this.

Table 1: Potential Net Migration Index (PNMI) and Nominal Tax Rates (NTR)

Country	PNMI Indicator	NTR Indicator
New Zealand	231%	33%
Singapore	225%	22%
Iceland	208%	46.24%
UAE	204%	0%
Switzerland	187%	40%
...	...	...
Nigeria	-46%	24%
Congo	-50%	35%
Syria	-44%	7%
Senegal	-34%	11%
Sierra Leone	-70%	5%

The results presented in the table show a slight correlation between the PNMI and the NTR. However, in our opinion, the problem of brain drain is still closely intertwined with tax issues both in the original country of residence of the individual and in his new jurisdiction. As Mohapatra (2012, 1) notes “the emigration of workers, especially high-skilled workers, is often perceived to create a fiscal loss – when considering the cost of educating these workers and foregone tax revenues for the home country.” Global challenges require global solutions, therefore, this article is focused on the search and development of such global approaches to cooperation in the area of taxation, aimed at solving the abovementioned problem of brain drain and losses of tax revenues, and to streamlining the global approaches to taxation of income of mobile talented professionals.

2. BRAIN DRAIN IN RUSSIA AND SERBIA IN THE CONTEXT OF TAX RULES

2.1. Characteristic of the Brain Drain problem in Russia and Serbia

In addition to the common Slavic roots, the proximity of languages and cultures, the interweaving of historical destinies and, of course, the Orthodox faith, Russia and Serbia are united by the brain drain problem. This issue was recognized by the Serbian President Aleksandar Vučić as a “serious” inhibitory factor in the development of the Serbian economy (*B92* 2019). In particular, the results of the study conducted by the Institute for Development and Innovations claim that losses stemming form from emigration of Serbia’s young people abroad cost the country 1.2 billion euros per year (about 2% of Serbian GDP), which is comparable to the amount of exports of IT services or agricultural products (*N1* 2019). IMF statistics say that around 50,000 people left Serbia in 2018 (*RTS* 2019). The results of a study conducted by RANEPA indicate a real increase in skilled emigration from Russia, although this is not about “the annual departure of millions, or even hundreds of thousands of people”. According to the calculations, around 100 thousand Russians emigrate to developed countries every year, of which around 40% have higher education (*RBC* 2018).

Is the tax burden important when the Russian and Serbian “brains” decided whether to emigrate? An analysis conducted by Chernykh (2018) regarding drivers for relocating IT specialists abroad indicates that career factors (“decent wages”, “interesting projects, career prospects”) have crucial importance for leaking brains, but comfort factors (“climatic conditions”, “good ecology”) are also important. A tax motivation does not play a significant role in deciding to emigrate. The main motivations of the drain of Serbian “brains” are also classic – according to *RTS* (2015) – it is “high unemployment, low incomes, and insecurity”.

2.2. Assessment of the Scale of Tax Losses from Brain Drain in Russia and Serbia

The results of the calculation of tax revenue losses from the brain drain are presented in Table 2. We use presume that emigrating workers earn an average salary at the highest level, so we calculated the potential personal income tax revenues from taxing such wages based on the statutory personal income tax rates of 12% and 13% for Serbia and Russia, respectively.

Table 2. Tax revenue losses from brain drain

Index	Russian Federation	Republic of Serbia
Number of emigrants per year	~100,000 (*RBC* 2018)	~50,000 (*RTS* 2019)
Average salary (highest)	51,000 RUB (Federal State Statistics Service 2017)	104,000 RSD (Statistical Office 2018)
Amount of tax losses from the brain drain	~7.95 bln. RUB.	~ 6.24 bln. RSD
Amount of collected personal income tax	~ 3301 bln. RUB (Federal Tax Service 2018)	~ 122.9 bln. RSD (Ministry of Finance of Republic of Serbia 2019)
Share	0.24%	5.07%

These calculations do not take into account indirect benefits for the donor country such as transfer of skills or remittances to family members of the emigrating individual; however, we suggest that even such simple estimation can indicate that the scale of the tax losses from the brain drain is much more significant in Serbia than in Russia. For the Russian Federation the indicator of net tax losses is not significant, not exceeding even 0.5% of personal income tax revenues, while for the Republic of Serbia the brain drain can even seriously affect the collection of personal income tax.

2.3. Comparison of Criteria for Tax Residence of Individuals in Russia and Serbia

Art. 207 of the Tax Code of the Russian Federation (hereinafter – the Tax Code) establishes the general rule for an individual to be considered to be tax resident of Russia, which is their actual physical presence in Russia for at least 183 calendar days of the calendar year[4]. Residents are subject to tax in Russia on their worldwide income and nonresidents are only taxed on incomes derived from the sources in Russia.

[4] This criterion is not the only one. Among other, secondary criteria, one can single out the recognition by tax residents of the Russian Federation of Russian military personnel serving abroad, as well as employees of state authorities and local self-government bodies sent to work outside of the state, regardless of the actual time spent in the Russian Federation.

Serbian residents are also subject to tax in Serbia on their worldwide income and nonresidents are subject to tax on Serbian-source income only. However, the Russian approach is different from the Serbian in the criteria for determining the residence of individuals. The key difference is that in addition to the objective criteria ("quantitative-day" factor), the Serbian tax legislation also establishes a subjective criteria for the tax residents of individuals, which is having domicile, residence or center of business and life interests in Serbia.

"Individuals are considered to be resident for tax purposes if they have a domicile, residence or center of business and life interests in Serbia or if they spend more than 183 days within a 12-month period, which begins or ends in the tax year (i.e. the calendar year)" (EY 2018a).

In the context of brain drain we can suggest that a stronger personal tax nexus to jurisdiction, which we can see in the Serbian legislation, is probably more beneficial for the donor country because it will allow such country to continue taxing the income of emigrants or remote workers because they are still Serbian tax residents on a worldwide basis. However, as follows from the analysis below, such a taxation possibility can be limited by tax treaties. On the other hand, the simplicity of the Russian tax residence rules for individuals can potentially limit the potential tax base of the state, not allowing it to continue taxing the income of emigrants or remote workers. According to the Ministry of Finance of the Russian Federation (2019), there is currently an intensive discussion in Russia about reforming the individual tax residence criteria in the direction of introducing subjective criteria such as the center of vital and business interests and/or by reducing the required period of physical presence in the country to 90 days. Such reform is intended to tighten the personal income tax residence criteria in Russia and to broaden its tax base.

3. ANALYSIS OF SPECIFIC CASES OF BRAIN DRAIN

Two types of rules that allow countries to tax individual income can be distinguished in the framework of the current approaches to taxation of the income of mobile and qualified individuals. First, these are the rules characterizing the personal nexus of an individual to the country, i.e. the rules of tax residency. Second, these are the rules characterizing the territorial nexus of income, establishing the criteria for income received from sources in the given country. As mentioned above, the current instruments of tax coordination, in relation to the taxation of income of migrant individuals (system of bilateral double tax treaties), mainly focus on the problem of eliminating double taxation by resolving potential conflicts through special rules. Such conflicts, according to

Holmes (2007, 23–24) can be residence-residence, residence-source or source-source. So, tax treaties restrict the rights of countries to tax the income. Such limitations of countries' taxing rights are reflected in the respective bilateral double tax treaties.

We analyze cases of brain drain typical for Russia and Serbia on the examples of an IT specialist, an athlete and a researcher, in the context of the existing international tax architecture and describe possible directions for the development of international tax cooperation in the field.

3.1. IT Specialists

3.1.1. Treaty Provisions Related to Income from Employment

The authors' analysis below relates not only to classical IT specialists (such as, for example, software developers) but also to the broader list of professions characterized as the remote workforce. In today's digital world, fewer and fewer professions require physical presence in the office. For example, this statement is almost 100% likely to be related to the activities of beauty-bloggers/vloggers/travel-bloggers, entrepreneurs, foreign language teachers, designers, writers, etc., because such professionals can work from anywhere in the world. This process has even led to the emergence of the concept of the "digital nomadism" and taxes are one of the main issues that both nomads and the state face, according to Kostic (2018, 191). Article 15 of the OECD Model Convention (OECD 2017a), Income from Employment, and Article 15 of the UN Model Convention (United Nations 2017), Dependent Personal Services,[5] set the rules for the elimination of double taxation of cross-border income of such a mobile workforce:[6]

1. Subject to the provisions of Articles 16, 18 and 19, salaries, wages and other similar remuneration derived by a resident of a Contracting State in respect of an employment shall be taxable only in that State unless the employment is exercised in the other Contracting State. If the employment is so exercised, such remuneration as is derived therefrom may be taxed in that other State.

2. Notwithstanding the provisions of paragraph 1, remuneration derived by a resident of a Contracting State in respect of an employment

[5] Hereinafter, the OECD Model (2017) and UN Model (2017) adopt the OECD and UN Model Tax Conventions. The following abbreviations are used when referring to the UN and OECD Model Conventions: OECD MTC, OECD MC, UN MTC, UN MC.

[6] Article 15 (paragraphs 1–2) of the OECD Model Convention is given. In our opinion, paragraph 3, which, for example, separately regulates the taxation of income of aircraft crew members, does not apply to the current study.

exercised in the other Contracting State shall be taxable only in the first-mentioned State if:

(a) The recipient is present in the other State for a period or periods not exceeding in the aggregate 183 days in any twelve-month period commencing or ending in the fiscal year concerned; and

(b) The remuneration is paid by, or on behalf of, an employer who is not a resident of the other State; and

(c) The remuneration is not borne by a permanent establishment or a fixed base which the employer has in the other State.

So, in other words the Article 15 of the OECD MC (OECD 2017a) cited above sets the exclusive rights of taxation of the employment income by the state of the employer's residence in two situations:

– if employment is exercised in the state of the employer's residence (Article 15(1));
– if the employment is not exercised in the state of the employer's residence, but all three conditions mentioned in Article 15(2) fulfill: (a) worker does not spent more than 183 days in the country of treaty partner; (b) income is not paid by the employer resident in the country of treaty partner; (c) income is not paid by the employer's PE or fixed base in the country of treaty partner.

In any other situations as prescribed by the Article 15(1) source country can tax such income and its taxing rights are not limited.

What is more, in some situations income of the remote workers can potentially fall in the scope of the Article 14 of the UN Model Convention (United Nations 2017), which covers income from "professional services and other activities of an independent character".[7] The fate of this article is very dramatic. Although it has been removed from the OECD Model Convention for various reasons[8] and is not affected by the Base Erosion and Profit Shifting (BEPS) Multilateral Convention, it is present in various forms in the actual tax treaties including both Russian and Serbian double tax treaties.[9] Here is this article from the UN Model Convention (United Nations 2017):

[7] Article 14 (2) of the OECD MTC (2017a) does not define what "professional services" are, but the commentaries to it note that they "particularly" include "independent scientific, literary, artistic, educational or teaching activities as well as the independent activities of physicians, lawyers, engineers, architects, dentists and accountants." The commentary to the article adds that this list is not exhaustive and that any difficulties in applying this paragraph may be resolved through a mutual agreement procedure.

[8] In fact, one key reason is that Article 14 of the UN Model Convention (2017) may well be covered by Article 7 Business profits.

[9] See, for example, double tax treaties that were concluded between the Russian Federation and Germany (1996), or between Bulgaria and Republic of Serbia (1998).

1. Income derived by a resident of a Contracting State in respect of professional services or other activities of an independent character shall be taxable only in that State except in the following circumstances, when such income may also be taxed in the other Contracting State:

(a) If he has a fixed base regularly available to him in the other Contracting State for the purpose of performing his activities; in that case, only so much of the income as is attributable to that fixed base may be taxed in that other Contracting State; or

(b) If his stay in the other Contracting State is for a period or periods amounting to or exceeding in the aggregate 183 days in any twelve-month period commencing or ending in the fiscal year concerned; in that case, only so much of the income as is derived from his activities performed in that other State may be taxed in that other State.

In the other words, Article 14 of the UN MC (UN 2017), cited above, sets the exclusive rights of taxation of the country of residence of the provider of professional services or other activities of an independent character unless there is either (1) a fixed base of such a service provider in the treaty partner state, or (2) time of stay of such a service provider in the treaty partner state is more than 183 days during a calendar year.

3.1.2. Offshorization or Emigration of the Workforce: Is Serbian Tax Base More Protected Against Erosion Than the Russian?

3.1.2.1. Offshorization of the Workforce

Let us consider the following case of the offshorization of the workforce. A Russian citizen and its tax resident, highly-qualified IT specialist, Evgeniy Kaspersky, decided to become a “digital nomad” starting from 1 April 2019. In April 2019, Evgeniy decided to leave Russia and settle in Cyprus, from where he continued performing his job duties for his Russian employer until the end of 2019. Such offshorization can be potentially motivated by corporate tax planning reasons. For example, the management of the Russian-based IT corporation can decide to locate at its subsidiary in Cyprus the development, enhancement, maintenance, protection and exploitation (DEMPE) functions, in relation to important intangibles. This can be done in order to bridge the gap between the corporate and economic structure of the multinational entity (MNE) group and to comply with the post-BEPS transfer pricing requirements (OECD 2015a, 13).

By applying the double tax treaty between Russia and Cyprus[10] to this case we can make observation that Russian taxing rights for such income from employment will be limited under Article 15 of Russia-Cyprus double tax treaty, which is based on Article 15 of the OECD Model, with exception of paragraphs (3) and (4) which relate to building sites, construction, assembly, or installation, to journalists and to employment exercised onboard ships. Therefore, Russia cannot tax such income for two main reasons: first, Evgeny ceases to be Russian tax resident, so both under Article 15(1) and 15(2) Russia cannot tax his employment income as the residence state; second, the employment is physically exercised in Cyprus and not in Russia, so under Article 15(1) Russia cannot tax such income as a source state either.

Let us assume that his Serbian colleague Borislav Djordjević made the same actions – moved to Cyprus and started working remotely for his home-country employer, from February to the end of the calendar year. It should be emphasized that in this situation the rights of the donor country to tax the income from employment are not limited by a tax treaty in case of such a remote worker who still has "vital interests" in the Republic of Serbia (family members and a house in Belgrade) and therefore remains a tax resident of Serbia. We shall also take into account that the residence-residence conflict can be potentially resolved under Article 4(2)[11] in favor of Serbia because such a person can have permanent homes available in both states, and personal ties with Serbia are stronger. Serbia can tax such income as the state of residence even if the employment is physically exercised in Cyprus and not in Serbia.[12] Cyprus also can tax such income from employment because timing condition from Article 15(2(a)) ensuring the exclusive right of the residence state to tax income from employment exercised in the other state is not fulfilled in this case. However, if such income was taxed in Cyprus it is exempt in Serbia, under Article 23(1(a)),[13] because this article uses the exemption method for the elimination of double taxation.

At the same time, if such a remote worker were to cease to be a Serbian tax resident, for example, if he sells house in Belgrade and his family moves to Cyprus, then the rights of Serbia to tax such income would be limited under Article 15 of the tax treaty for the same reasons

[10] Agreement between the Government of the Republic of Cyprus and the Government of the Russian Federation for the avoidance of double taxation with respect to taxes on income and on capital (1998)

[11] Convention between the Republic of Cyprus and the Socialist Federative Republic of Yugoslavia for the avoidance of double taxation with respect to taxes on income and on capital (1985)

[12] *Ibid*.

[13] *Ibid*.

as in Russian case above – the employment is not physically exercised in Serbia.

So, we suggest that the Serbian tax base is more protected from the erosion resulting from such offshorization of its workforce than the Russian tax base. However, if such income of the remote employer is taxed in the recipient country, the results are the same for the both states – they lose tax revenue because the recipient country has a priority right to tax such income.

3.1.2.2. Emigration of the Workforce

Let us consider the case of the emigration of the skilled workforce. A Serbian citizen and its tax resident, highly-qualified IT specialist Stefan Ibrahimović, decided to work for UK company starting on 1 April 2019. In April 2019, Stefan leaved Belgrade and settled in London, from where he continued performing his job duties for his UK employer until the end of 2019. Such emigration can be potentially motivated with classical combination of the reasons: quality of life, better career prospects, higher salary, etc. Let us also look at tax consequences of the same scenario performed by his Russian friend Mahomed Burkhanov, who migrated from Moscow to London to work for the same UK company in March 2019 and continued working their until the end of the year.

In this situation, the results of application of the double tax treaty[14] in the case of the Russian emigrant are the same as in the case above for the offshorization of the workforce – Russia loses its taxing rights and its tax base. For Serbian emigrant, the results are also the same as in the case above.[15] Serbia can tax employment income of its resident as long as it considers the emigrant to have strong personal nexus with Serbia. Such nexus can be evidenced by the home available to him in Serbia and the center of business and life interests in Serbia. So, potential residence-residence conflict will be resolved in favor of Serbia under Article 4(2).[16] The only difference from the previous scenario is that if the UK also taxed such employment income, such tax would be credited against the Serbian tax, but not exempted as was the case in the previous example, because the Yugoslavia-UK double tax treaty (DTT)[17] contains the credit method for the elimination of double taxation.

[14] Convention between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the Russian Federation for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and capital gains (1994)

[15] Convention between the United Kingdom of Great Britain and Northern Ireland and the Socialist Federative Republic of Yugoslavia for the avoidance of double taxation with respect to taxes on income (1981)

[16] *Ibid.*

[17] *Ibid.*

3.1.3. Interim Conclusion

We can conclude from the analysis above that economically the tax consequences of the migration and offshorization of the workforce from Russia and Serbia are almost the same – the donor countries lose their personal income tax base (taxing employment income) and give the recipient countries the priority rights to tax such income. Such tax policy outcomes can potentially result in the losses of tax revenues from personal income tax by the countries suffering from the problem of the brain drain.

3.2. Athletes

The Russian Federation is known all over the world for its athletes. For example, at the 2016 Summer Olympics, the Russian national team was at the 4th place and the Russian national football team reached the quarter-final at the 2018 FIFA World Cup. Serbian representatives of sports are also very famous all over the world. These are the names of Novak Djoković, Ana Ivanović, Jelena Janković, Vlade Divac, Branislav Ivanović, Sinisa Mihajlović and others. As experts note, in individual sports (although, in our opinion, this is also possible in team sports), the change of tax residence for the purpose of tax planning is a very common practice. For example, Gatto (2017) suggest that as of 2017 such well-known tennis players as Novak Djoković, Caroline Wozniacki, Marin Čilić, Petra Kvitová are residents of Monaco, Borna Ćorić, Karen Khachanov and Svetlana Kuznetsova are UAE residents. Each of these countries does not levy taxes on the income of individuals and has very flexible tax residence requirements.

Such tax policy practices can be analyzed in the context of criteria developed in the OECD's work on harmful tax competition (OECD 2015b) because they can potentially lead to the losses of tax base by the other countries which have strong personal nexus with such individuals and can be potentially described as "tax residence for sale". Such practices erode the foundation of tax law because they in fact regard legal rights and tax sovereignty – the concepts that cannot by definition have market value – as market commodities and shift the line between those residents who get residence status by buying it or investing in the country's economy and other persons who get this status resulting from personal inherent nexus with the state (Thirion, Scherrer 2018).

Prevention of double taxation of cross-border income of "entertainers and sportspersons" is regulated by Article 17 of the OECD Model Convention (OECD 2017a), which contains two paragraphs. The first one states that "notwithstanding the provisions of Article 15, income derived by a resident of a Contracting state as an entertainer, such as a theatre, motion picture, radio or television artiste, or a musician, or as a

sportsperson, from that resident's personal activities as such exercised in the other Contracting State, may be taxed in that other State." The second paragraph, states that "where income in respect of personal activities exercised by an entertainer or a sportsperson acting as such accrues not to the entertainer or sportsperson but to another person, that income may, notwithstanding the provisions of Article 15, be taxed in the Contracting State in which the activities of the entertainer or sportsperson are exercised."

However, what income and what share of it may be taxed by the state hosting the sporting event under Article 17(1) of the OECD MTC? The answer to this question is contained in the commentary to Article 17 of the OECD MTC (2017a) relating to the taxation of "entertainers and sportspersons". Paragraph 8 of the commentary states the following: "Paragraph 1 applies to income derived directly and indirectly from a performance by an individual entertainer or sportsperson. In some cases the income will not be paid to the individual, or his impresario or agent, directly with respect to a specific performance. For instance, a member of an orchestra may be paid a salary rather than receive payment for each separate performance: a Contracting State where a performance takes place is entitled, under paragraph 1, to tax the proportion of the musician's salary which corresponds to such a performance." Although this passage mainly refers to artists, it is safe to assume that the same approach can be applied to the salaries of athletes.

As the commentators further note, entertainers and athletes often earn royalties, sponsorships or advertising fees. Where there is a close relationship between the income received and the activities carried out in the country, the host State is also entitled to tax the income. The determination of the level of such relationship can be made on the basis of an analysis of the "timing of the income-generating event," the "nature of the consideration for the payment," and the "contractual arrangements" for participation in such events. Finally, the provisions of Article 17 may also apply to the taxation of remuneration for the time spent on "rehearsal, education or similar training" of athletes in the receiving State.

The distribution of the taxing rights of athletes' income between two countries that have a tax treaty depends on the jurisdiction in which the athlete is a tax resident, as well as on the state in which the sports activities are carried out. Based on this idea, we suggest the borderline scenarios where the donor state loses its tax revenues resulting from athletes' brain drain.

The state drastically loses the right to tax the athlete's income if:

- the athlete ceases to be a tax resident of this State;
- the athlete is not a participant in events taking place in this State.

In our opinion, this risk is more significant for the tax system of the Russian Federation, which uses only a simple "quantitative and daily" approach to determining whether an individual is a tax resident of the state.

3.2.1. "G" Case: How to Lose the Right to Tax the Income of a "Draining Feet"?

Let's consider the relationship between Russian tax legislation and tax treaties in the context of brain drain on an example from professional football. Let us assume that at the end of July 2018, Russian midfielder of FC SKA (Moscow), Alexander G., joined FC Amateur from the Principality of Monaco. Prior to joining the foreign club, Alexander was a tax resident of Russia. Most of the player's matches and training process took place in the Russian Federation. Therefore, it can be stated that regular income from the player's sporting activities was taxed in the Russian Federation, at a rate of 13%.

Let us assume that at the end of August 2018 Alexander G. received his first income from a foreign football club. Probably, the athlete is not yet a tax resident of Monaco, as he has not spent enough time in the Principality. On the other hand, the athlete is likely to be recognized as a tax resident of the Russian Federation at the end of 2018, as he has spent more than 183 days in the country that year. Thus, our hero will have to calculate and pay personal income tax at the rate of 13% on his own, as well as submit a personal income tax return to the tax authority where he resides, no later than April 30 of the following year.

Due to the large number of matches in the French championship (FC Amateur is a rare example of a football club that plays in a foreign league), the athlete begins to visit the Russian Federation less and less often. Let's assume that for the whole year of 2019 the period of his stay in the state was 45 days (vacation and a stay in the national football team). Then, with a high degree of probability, we can conclude that, for the fiscal year 2019 Alexander G. will cease to be a tax resident of the Russian Federation, and so Russia will lose the right to tax his income. There is an example of "draining foot". Additionally, if the athlete becomes a tax resident of Monaco, his income will be taxed at a zero rate.

3.2.2. "Branislav" Case: How Can the Russian Federation Tax the Foreign Player's Income?

As we see from the example above, Russia can easily lose the tax revenue from the taxation of income of its talented sportspersons if they cease to be Russian tax residents. In this section we analyze possible scenarios of taxing a foreign footballer's income in Russia.

The most obvious situation is if any foreign athlete become a tax resident of the Russian Federation. This is very likely scenario, because Russia is not only exporter but also an importer of the football talents. Many of the world stars have been playing for a long time in the Premier League: for example, Branislav Ivanović and André Schürrle.

The second scenario is of a foreign club to arrive to Russia for a tournament match. As mentioned above, the host country may tax the relevant part of the salary, as well as royalties, sponsorships or advertising fees, which are closely related to the activities in the respective country. For the situation in question, such income may include the remuneration for the interview given by the player during the tournament, or the fee for the use of their photo on the posters inviting fans to the match. Let's assume that attacking player of the Italian football club FC Sardinia Bronislav Stanley arrived with his team to play a match against Moscow-based FC Berezovsky. Bronislav is obviously not a tax resident of the Russian Federation, so his income will be taxed at a higher rate of 30%, rather than 13%, which can potentially result in an additional increase in tax revenue for Russia. However, in our opinion, this is the end of the positive aspects of the current mechanism of taxation of athletes arriving solely for sporting events. First, the mechanism of tax collection from a foreign athlete is absolutely incomprehensible.[18] Secondly, the probability of a particular club coming to Russia is not the highest. Third, it is unlikely that the potential amounts can be comparable to the full taxation of the income of an athlete with the status of a tax resident of the Russian Federation.

As noted above, under Serbian national legislation, an individual may also be recognized as a tax resident on the basis of subjective criteria. Probably such an approach protects the tax base of the Balkan country from eroding, but only with the limited extent. Let us turn once again to the case study of tennis player Novak Djoković, in particular to one of his more recent interviews (Gatto 2018) in which he said that the choice in favor of Monaco was made due to the "beauty" of the Principality. He stated that he has a house in which his wife and children live, as well as his current and former coaches in this beautiful country – the presence of such conditions allows Novak Djoković to "fully focus on tennis." If we assume that Novak can be considered a tax resident of Serbia, we would probably be wrong. First, the tennis player does not meet the "quantitative and daily" criterion of at least 183 days of the physical presence in Serbia (which is likely, considering the traveling lifestyle of the athlete). The

[18] "Dear Lionel Messi! You have to register for tax purposes in Serbia, because you participated in a friendly match between the Serbia and Argentina. We do not know what part of your income we will tax, but we are still waiting for you with a full set of documents at 5 Save Maskovica Street, Belgrade". In our opinion, this situation absolutely fantastic!

analysis of the subjective criteria also shows that center of his vital interest is more likely in Monaco because his home and family live their indicating his strong personal ties to the Principality.

3.2.3. Athletes in the Digital Age: The Case of Non-Taxation

In the context of the challenges of the digitalization of the economy and brain drain, another potential problem should be mentioned, which is at the intersection of sport and entertainment. Let us turn to one piece of recent news (Grace 2019):

> "Electronic violinist Lindsey Stirling is putting on a new kind of interactive virtual concert, performing live to fans in avatar form. The concert, put on in collaboration with streaming platform Wave, will take place at 3 p.m. (EST) on Monday 26 August. Stirling will perform through her avatar, powered by art body motion and face capture technology. Fans will also be able created their own avatars and attend the virtual show by downloading the Wave virtual reality (VR) app, supported by HTC Vive and Oculus Rift. Throughout the concert, Stirling will interact with fans 'in a variety of direct, mysterious and surpris[ing] ways.' Limited edition concert merchandise will be available to buy."

Based on the content of this news we imagine the following case. Suppose that we have two young athletes – a Russian citizen, resident of the Russian Federation, Anton, and a citizen of the Republic of Serbia and its tax resident, Branka. Both are recognized ice skating masters. In 2019 our heroes decided to end their professional sport careers and form a duo to perform colorful ice shows. While devising their marketing strategy, the young athletes turned to the fast-evolving "augmented reality" technology, which allows them to create unique special effects for the audience. This choice also allowed new entrepreneurs not to be physically present in other countries, which greatly facilitated the working conditions for both themselves and the support team.

Based on this logic, the athletes relocated to the small jurisdiction Y, with which both Russia and Serbia have double tax treaties in force. The legislation of state Y offers low rates of personal income tax, as well as simple criteria for determining the residence of individuals (stay in the state Y for 90 days during a calendar year and a "permanent home available"). Finally, country Y is characterized by the availability of cheap and qualified labor and a large number of free ice rinks. In order to replenish the seed capital and to buy real estate in State Y, both Branka and Anton sold their apartments in Belgrade and in Moscow, respectively. Thus, at the beginning of January 2019, our heroes left for jurisdiction Y to settle all the legal issues and practice the "virtual" show. In October

2019, the production was triumphantly launched and broadcast to a large number of viewers, including in the Russian Federation and Serbia. The project is monetized through selling the online advertisement space during the online broadcasting aimed at target groups from Russia and Serbia.

What "piece of the tax pie" can Russia and Serbia claim? Admittedly, it is a small one or even none. It is likely that in 2019 Anton will not be recognized as a tax resident of the Russian Federation and Branka will not be recognized as a tax resident of Serbia due to the "quantitative factor" and the sale of real estate in Belgrade. Physically, our young "athletes" did not travel to the two countries for performances, which severely limits the possibilities for taxation although the fact that the "virtual" value was created in the source countries is obvious.

3.2.4. Interim Conclusion

We can conclude from the analysis above that generally tax treaties do not limit countries' rights to tax the income of the athletes while the athletes are their tax residents. If an athlete ceases to be a tax resident of the country, which is a common scenario in the context of brain drain, then the donor country loses its right to tax the income of such athlete until he physically arrives and take part in sporting events in the country.

The change of tax residence can be also accompanied by harmful tax competition between the jurisdictions, ultimately leading to so-called "tax residence shopping", which is especially relevant for individual star sportspersons who earn very huge amounts of income. If we consider that such sportspersons are often born, raised and trained in developing countries, where they took their first steps as a professional sportspersons, we come to the conclusion that the non-taxed income of such sportspersons is in fact the tax base of such donor countries lost due to brain drain.

Furthermore, our analysis shows that the rule in Article 17(1) allowing the host country to tax part of athlete's income from sports events in this country is impractical and generally useless, because the administrative costs of the implementation of the taxation mechanism for such income and allocation of the appropriate tax base can outweigh the tax benefits received; this rule is also not in line with the process of the digitalization of entertainment and sports content.

3.3. Academics and Scientific Researchers

Besides its achievements in the area of professional sports, the Russian Federation is famous throughout the world for its activities in the field of scientific research. For example, according to the rating of publishing activity by Scimago Journal & Country Rank (2018)[19], the

[19] See: Scimago Journal & Country Rank. *https://www.scimagojr.com/countryrank.php?year=2018* (last visited 6 October 2019).

Russian Federation ranks 11th, and according with the rating QS World University Rankings (2019)[20] there are currently 27 Russian universities in the world top-1000 list. The rankings of the Republic of Serbia on the same lists are following: the country holds the 54th place in the first nomination and only one Serbian university – the University of Belgrade – is in the list of top-1000.[21]

How do these brain drain statistics in the field of research and education relate to the countries' fiscal interests? The basic tax policy idea can be to expand tax jurisdiction to the widest extent possible in order to try on the one hand to secure the right to tax the income of researchers leaving the country and on the other hand to tax foreigners arriving in the country. The balance between these two tax policy goals can depend on the net balance of export and import in the areas of research and higher education. However, tax policymakers can have also other considerations and use other taxing approaches towards income of researchers. For example, the positive social and economic impact of research and education on the wider society can be considered, therefore countries can exempt from taxation the income of researchers, such as research grants.

3.3.1. Taxation of Academic Researchers' Income Under the OECD and UN Models

Both the OECD MC and the UN MC do not contain separate articles addressing the issues of double taxation of the income of academic researchers (professors, lecturers, etc.). However, we cannot claim that this issue was historically ignored by the academic community. It is presumed that this issue is covered by the provisions of articles 14 (in case of providing independent personal services), 15 (dependent personal services), 19 (if remuneration is paid by the one of the negotiating states) in case of the UN MC (United Nations 2017, 452). However, "it was noted that articles 14 and 15 commonly did not exempt a visiting teacher's compensation from taxation at source because they generally allowed source taxation of service performers who were present in the host country for more than 183 days, and many teaching assignments exceeded that period of time" (United Nations 2017, 452).

At the end of the 20th century experts proposed to amend the UN MC and to add a separate article covering the issues of double taxation of income of "visiting teachers". However, there was no consensus regarding such provisions, so the discussion ended in the compromise decision: not to make amendments into the Convention but to amend the Commentaries

[20] See: QS World Universities Rankings. *https://www.topuniversities.com/university-rankings/world-university-rankings/2019* (last visited 6 October 2019).

[21] *Ibid*.

to the Convention, explaining that double tax treaties can potentially have such special articles and some guidance regarding the contents of such articles in case of having bilateral discussion about the issue (United Nations 2017, 453):

- The purpose of a tax treaty generally is to avoid double taxation, and double exemption of teachers is not desirable,
- It is advisable to limit benefits for visits with a maximum duration (normally two years), and the time limit should be subject to expansion in individual cases by mutual agreement between the competent authorities of the Contracting States,
- Whether the benefits should be limited to teaching services performed at certain institutions "recognized" by the Contracting States where the services are performed,
- Whether, in the case of visiting professors and other teachers who also do research, to limit benefits remuneration for research performed in the public (vs. private) interest,
- Whether an individual may be entitled to the benefits of the article more than once.

If we observe the real networks of bilateral tax treaties of the analyzed countries we can say that the draft provisions proposed by the OECD MC (OECD 2017a) are not accepted as a rule by both the Russian Federation and the Republic of Serbia. There are plenty of double tax treaties of which Russia is a part where taxation of scientific researchers is regulated by a separate article or an article similar to the article contained in the UN MC (United Nations 2017). One example is the double tax treaty between Serbia and Bulgaria[22] where the issue of double taxation is regulated by Article 21 Professors and Scientific Researchers, which contains the following provisions:

1. An individual who visits a Contracting State for the purpose of teaching or carrying out research at a university, college, school or other recognized educational institution in that State and who is or was immediately before that visit a resident of the other Contracting State, shall be exempt from taxation in the first-mentioned State on remuneration for such teaching or research for a period not exceeding two years from the date of his first visit for that purpose, provided that such remuneration is derived by him from outside that State.

2. The provisions of paragraph 1 of this Article shall not apply to income from research if such research is undertaken not in the public

[22] See: Convention between the Government of the Republic of Bulgaria and the Federal Government of the Federal Republic of Yugoslavia for the avoidance of double taxation with respect to taxes on income and on capital (2000).

interest but primarily for the private benefit of a specific person or persons.

The provisions of Article 21 of Serbia-Bulgaria DTT precludes the recipient state from taxing the income received by the newly-arrived professor or scientific researcher, but only if such income is derived from sources outside that recipient state. Such an approach protects income of the "drained brain" from being taxed at the place of their migration if such academic migration or travel is financed by a source outside the recipient state. At the same time such an approach does not shield donor state from tax revenue losses in cases when such academic travel or migration is financed by the recipient state. These scenarios and the effects of double tax treaties in the context of brain drain are illustrated by the two cases below.

3.3.2. Case 1: Scientific Researcher Leaves the State and Receives Financing from This State, Donor State Is Temporarily Protected from Loss of Tax Revenues

A teacher of the Serbian language at the local university, Jovana B., a resident of the Republic of Serbia, moves to country Y with the aim of popularizing the Serbian language among the students of the local university. The academic trip is financed from the grant program financed by the Serbian university and lasts for the period of one year. There is a double tax treaty between the Republic of Serbia and country Y with the same provisions as in Article 21 of the Serbia-Bulgaria DTT.

We can conclude that the income of Jovana B. will not be taxed in country Y. If Jovana B. is still a tax resident of the Republic of Serbia, her income will be taxed in Serbia. Therefore, this example illustrates the "normal" scenario of the application of such a provision. The effects in the context of brain drain are: (1) the donor country does not lose its revenues for the period mentioned in the DTT, (2) however, the donor country can still lose its revenue if Jovana's academic trip lasts for more than one year because she will likely not be regarded as tax resident of Serbia, therefore in this case double non-taxation can arise.

3.3.3. Case 2: Scientific Researcher Leaves the Country Financed by the Recipient Country

Let us now assume that, as in the previous case, Jovana moved to the same country Y with the same academic purpose, but in this example her academic visit is financed by country Y. In this case provisions of Article 21 of the DTT, similar to Article 21 of the Serbia-Bulgaria DTT, would not prevent the recipient country from taxing her income because it is sourced outside of the Republic of Serbia. However, such income can

also be taxed in Serbia for as long as Jovana is a Serbian tax resident. So, the issue of double taxation can arise, which will be resolved under the relevant DTT Article on double tax relief. However, the recipient country will have priority right to tax the income and the donor country (Serbia in this example) will be providing relief in the form of credit or exemption.

3.3.4. Interim Conclusion

We can conclude that donor countries can potentially lose the right to tax foreign sourced income of emigrating researchers who are moving to conduct their research and teaching activities abroad, if such relocations are financed by the recipient country.

We also propose the idea for the design of separate article in the UN MC devoted to taxation of researchers and visiting teachers. We believe that in such an article only the country financing the research project or visit should have the exclusive right to tax such income, irrespective from the period of the research visit. We propose such idea because: (1) academic research is usually conducted for public benefit, so we can deliberately create the possibility for individual countries to exempt such public good from taxation if they wish so (Pigouvian subsidy argument) (Pigou 1920); (2) experienced researchers can be very mobile, engaging in projects around the world, so it is more convenient to tax their income based on the source rather than the residence principle.

Application of the tax treaties based on the UN and the OECD models can lead to double non-taxation and inconsistencies between the country of taxation and the country of real economic activity of mobile individuals. Therefore, we put forward the idea of the need to expand areas of global tax coordination aimed at minimizing and mitigating the negative consequences of the migration of the qualified specialists from less-developed countries to more-developed countries, as well as creating global tax rules that would not create additional artificial incentives for migration and would not lead to an unfair loss of tax revenues and resources by human capital donor-countries.

4. BEOGRADSKI EPOHALAN POREZNI SPORAZUM (BEPS 2.0) OR POSSIBLE DIRECTIONS FOR DEVELOPMENT OF INTERNATIONAL TAX COOPERATION ADDRESSING THE BRAIN DRAIN ISSUE

4.1. Limits of International Tax Cooperation in the Area of Brain Drain

In this paragraph we stress the necessity for the rethinking the design of international tax law in the complex, cohesive and multilateral way, with

the aim of aligning the place of taxation with the place of talent creation and making some proposals for further advancement. On the one hand, the history of international relations contains a large number of examples of successfully concluded multilateral agreements. On the other hand, they are mostly limited to specific regional unions and are formed where there are economic, cultural or ethnic preconditions for their creation (Bravo 2016, 280). Moreover, according to some experts, multilateral mechanisms, including consensus between countries on certain tax issues, are a "utopian view of international tax law" (Schwartz 2015).

Broekhuijsen, Vording (2016, 43) highlights the following ideas in the context of global governance:

– (neo)realism – states are rational players in an anarchist world, and for any development, the initiative of the most developed countries is required;
– (neo)liberalism – states are subjects of relations for which economic rationality plays the most important role in participating in multilateral agreements – countries enter into multilateral cooperation only if they see this as an economic benefit that can be estimated.

It seems difficult to unambiguously determine which of the strategies is dominant in the context of tax cooperation for the purpose of combating the brain drain. On the one hand, the tax policies of the BRICs countries (Brazil, Russia, India, and China), especially China and India, whose opinion on tax issues may differ from the position of the OECD, are beginning to gain more weight in the global tax governance debate. On the other hand, the current international tax architecture is "under the umbrella" of the developed OECD countries, which are the main recipients of the "brains" from developing jurisdictions. This, in particular, is again indicated by the Gallup Institute data: out of 41 regions that have potential positive population growth in the scenario of a complete emigration of brains, 22 are developed countries that are members of the OECD:

Table 3: Jurisdiction structure with positive population growth[23]

Indicator	OECD countries	Other countries
Amount	23	18

[23] See: compiled by authors based on World Bank Data. *https://data.worldbank.org/indicator/ny.gdp.mktp.cdm* (last visited 25 September 2019), and Gallup Institute. *http://news.gallup.com/migration/interactive.aspx?g_source=link_newsv9&g_campaign=item_245204&g_medium=copy* (last visited 25 September 2019).

Share of GDP in global GDP	53.04%	2.57%
Potential Net Migration Index	83%	63%

Based on the results in Table 3, it can be presumed that the role of the developed OECD countries so far remains dominant in global coordination of taxation, which, in particular, is also indicated by the experience of drafting the multilateral agreement under BEPS (Byrne 2016). Therefore, assuming that brain drain is a positive process for recipient countries, it seems unlikely that there will be a radical transformation of the international tax architecture towards a certain redistribution of tax revenues in favor of developing countries suffering from the brain drain. That is why we consider ideas such as the Bhagwati tax (Bhagwati 1976, 34) to be utopian and unrealistic. However, we call for some form of global cooperation and some ideas for such cooperation are presented below.

We take into account the unprecedented scale of tax cooperation observed at the present. Despite the fact that initially researchers from different countries expressed some skepticism regarding the effectiveness of the implementation of the BEPS plan (can the idea of interstate tax cooperation for a more equitable tax collection be a significant incentive for jurisdictions?), as of 2019, it can be stated that the BEPS plan met its expectations at least retarding the rate of expansion of its ideas worldwide.

First, the qualitative and quantitative composition of the participant countries is surprising. As of July 2019, 132 jurisdictions are member states of Inclusive Framework on BEPS, including both developed (e.g. the USA, the UK) and developing countries (e.g., China, India) and typical offshore countries (e.g. British Virgin Islands, Belize, Barbados.).[24] A significant number of participants are also covered by the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS – “a king treaty” implementing BEPS measures into the actual double tax treaties. Despite the fact that Action 15 of the BEPS plan was not part of the so-called “minimum standard” of BEPS, 89 jurisdictions have already signed it (OECD 2019c).

Second, prior to the implementation of the BEPS plan, many countries aggressively used tax incentives for multinational corporations as part of their international tax policies (for example, having low tax rates for foreign sourced income in conjunction with no exchange of information). However, since the launch of the BEPS plan, the OECD has already analyzed 287 tax regimes, of which 76 were canceled, 11 were recognized as malicious or potentially harmful, 15 are in the process of

[24] See: OECD. What is BEPS? *http://www.oecd.org/tax/beps/about/* (last visited 26 September 2019).

cancellation/replacement, etc. (KPMG 2019b), which is the result of the BEPS Action 5 on harmful tax competition.

Of course, the BEPS will not stop international tax competition, as its scope does not affect all forms of tax incentives for attracting global capital. However, for the first time, countries have shown such global intention for international tax cooperation on the issue of non-taxation.

4.2. What Can We Pick from the BEPS Project for the Proposed BEPS 2.0?

In our opinion, some points of the BEPS Project are irrelevant for the proposed multilateral tax cooperation in the context of brain drain. These are Action 2 – Neutralizing the Effects of Hybrid Mismatch Arrangements, Action 3 – Controlled Foreign Company, Action 4 – Limitation on Interest Deductions, primarily because these actions relate to corporations and do not relate to individual income. We do not claim that the experience of these actions is generally not applicable to brain drain – rather, we can discuss the need for a more in-depth analysis. We propose some ideas of adapting the approaches developed under the BEPS Project for addressing the brain drain issue, presented in Table 4.

Table 4: Selected BEPS Plan Actions and their applicability to BEPS 2.0

<table>
<tr><th>Action</th><th>Scope of applicability</th></tr>
<tr><td>1 – Tax Challenges Arising from Digitalization</td><td rowspan="3">Improving the mechanism of income allocation in the context of the migration of talented individuals in the direction of more alignment between the place of taxation and the place of creation of value, which in the case of individuals is the place of “talent creation and skills development” and in the context of the digitalization of the economy is the place of virtual economic activity and economic presence</td></tr>
<tr><td>8–10 – Transfer Pricing</td></tr>
<tr><td>13 – Country-by-Country Reporting</td></tr>
<tr><td>5 – Harmful Tax Practices</td><td>Assessment of limits of acceptability of “aggressive tax incentives” employed by the countries in the processes of brain drain
Exchange of information relating to tax incentives for attracting “brains”</td></tr>
<tr><td>6 – Prevention of Tax Treaty Abuse</td><td>Improving the preamble to bilateral tax treaties in order to show countries’ intentions to not create opportunities for non-taxation of migrating individuals</td></tr>
<tr><td>11 – BEPS Data Analysis</td><td>Creating an internationally consistent methodology for assessing tax losses from brain drain</td></tr>
</table>

Action	Scope of applicability
12 – Mandatory Disclosure Rules	Disclosure of information about the level of tax burden on mobile highly-qualified individuals
14 – Mutual Agreement Procedure	Streamlining the mechanism of mutual agreement procedure for addressing the scenarios of “double residence” or “no residence” in the context of brain drain. The development of the concept of “vital interests” in relation to digital nomads
15 – Multilateral Instrument	Multilateral agreement for the synchronized implementation of anti-brain drain measures in bilateral tax treaties

4.2.1. Limits of the Acceptability of “Aggressive Tax Incentives” Employed by Countries in the Processes of Brain Drain and the Launch of a Spontaneous Exchange of Information on Incentives for Attracting “Brains” (Action 5)

Various socio-economic instruments can be used to combat “brain drain”. They also include measures to improve national tax policies – here are just a few recent changes:

- a reduction in the tax rate for young Poles with the intention to decrease the level of brain drain in Poland (Voice of America 2019);[25]
- the elimination of tax incentives for tax residents working abroad (Arendse 2019);[26]
- lowering the requirements for tax residence to increase win in tax competition for digital nomads (CNews 2018);[27]

[25] At the end of July 2019, the Polish government abolished the personal income tax for young Poles, imder the age of 26 years old and earning less than PNL 85,500 . As Polish Prime Minister Mateusz Moravecki noted, this decision was made in order to stop the brain drain from the country, the scale of which is very significant. Since 2004 between 1.5 and 2 million citizens left the country. According to experts, about 2 million people will be able to take advantage of this benefit. (Voice of America 2019)

[26] Previously, South African tax residents living and working abroad for more than 183 days (and more than 60 consecutive days) were exempted from paying the national tax on their foreign income, but starting from March 2020, this approach will change. The amendments will require South African specialists who reside and work abroad but are still considered “physically present” (quantitatively daily test) or “usually resident” (subjective assessment of “actions, connections and intentions”) in the country to pay tax to the South African state in the amount of up to 45% of their gross foreign income, provided that it exceeds ZAR 1 million. (Arendse 2019)

[27] In 2018, a draft law was discussed in Russia, according to which IT specialists spending more than 90 days a year in Russia can receive tax resident status. The changes are aimed at increasing the country’s tax attractiveness for traveling IT professionals,

Despite the different approaches, each of these cases represents the reaction of the states to the global process of the brain drain/brain gain. However, in our opinion, in addition to the cooperative struggle against aggressive corporate tax regimes, in the near future the international tax community may also require a similar "audit" of the provisions of national laws directly or indirectly aimed at attracting and retaining human capital. For example, the reasons for the expansion of tax sovereignty in the case of the Republic of South Africa may indicate its necessity: according to the competent authorities, the cancelled tax exemption was excessively "generous", especially in cases where an individual worked in a jurisdiction with an extremely low or zero personal income tax rate (e.g. UAE) (Arendse 2019).

Thus, the first issue at which such an audit should be directed is the delineation of cross-border situations in which brain drain can lead to non-taxation or reduced taxation, as well as a clear definition of the conditions under which the tax incentives provided by one country harms another country. When developing a methodology for determining the integrity of provisions in domestic tax legislation, attention should also be paid to criteria indicating the potential harmfulness of the preferential regimes outlined in the OECD report Harmful Tax Competition: An Emerging Global Issue (OECD 1998):

Table 5: A list of factors indicating the harmfulness of the preferential regime

Key factors	Other factors
No or low effective tax rates	An artificial definition of the tax base
"Ring-Fencing" of Regimes	Failure to adhere to international transfer pricing principles
Lack of transparency	Foreign source income exempt from residence country tax
Lack of effective exchange of information	Negotiable tax rate or tax base
	Existence of secrecy provisions
	Access to a wide network of tax treaties
	Regimes that are promoted as tax minimization vehicles
	The regime encourages purely tax-driven operations or arrangements

who, according to the new rules, will be able to pay income tax at a rate of 13% – one of the lowest income tax rates in the world. (CNews 2018)

This report includes a sequential set of three questions, the answers to which help determine whether the potentially harmful tax regime is actually harmful (OECD 1998):

- Does the tax regime shift activity from one country to the country providing the preferential tax regime, rather than generate significant new activity?
- Is the presence and level of activities in the host country commensurate with the amount of investment or income?
- Is the preferential tax regime the primary motivation for the location of an activity?

In addition to conducting continuous monitoring and spontaneous exchange of information about such regimes, by analogy with the recommendations of the Report (OECD 1998) and BEPS Action 5, we offer the following: after considering the economic consequences of the existence of preferential provisions in national legislation, such norms can be considered aggressive, and the country will have the opportunity to cancel or modify them by amending national tax legislation. In turn, other countries may take protective measures against the negative impact of such provisions, while also encouraging the possibility of adjusting or even denouncing them.

4.2.2. Unified Methodology for Assessing Tax Losses from Brain Drain (Action 11)

The magnitude of the BEPS problem in the corporate area is between USD 100 bln and USD 240 bln or between 4% and 10% of global corporate income tax (CIT) revenues (OECD 2015c, 15). In addition to significant financial losses, the BEPS process has other economic consequences, including, for example, tilting the playing field in favor of tax-aggressive MNEs, distorting the location of highly-mobile, intangible assets, misdirecting foreign direct investment, etc. (OECD 2015c, 15).

Therefore, in our opinion, monitoring the BEPS magnitude is one of the most important parts of the BEPS plan. As noted by the OECD, “the lack of quality data on corporate taxation has been a major limitation to measuring the fiscal and economic effects of tax avoidance as well as any efforts to measure the impact of the implementation measures agreed as part of the BEPS Project” and “increasing the quality of the data and the analytical tools available, through the ongoing work under Action 11, is crucial in being able measure the impact of tax avoidance and the effect of the implementation of the BEPS measures in curbing these practices.”[28]

[28] See: OECD. Action 11 BEPS data analysis. *https://www.oecd.org/tax/beps/beps-actions/action11/* (last visited 24 September 2019).

To date, the Inclusive Framework is actively working on this action of the BEPS Project. In particular, in January 2019, the Corporate Tax Statistics Database was launched, which stores data related to the BEPS process and the taxation of MNEs in general. Additionally, the first Inclusive Framework presented the first summary statistics based on an analysis of the results from the implementation of Action 13 on Country-by-Country Reporting.[29] Finally, the international organization notes that the workflow under Action 11 is too early to stop: the Inclusive Framework is developing "new and enhanced datasets and analytical tools that can assist in measuring and monitoring the fiscal and economic impacts of tax avoidance and the effects of the implementation of the BEPS measures".[30]

Unfortunately we cannot say that the international tax community has a similar level of analytical apparatus for assessing tax losses from a brain drain. Humanity does not fully understand the extent of tax losses from a brain drain, although it is intuitively clear that it is not much less than losses of USD 100 bln to USD 240 bln from tax avoidance by the corporations (this, for example, is indicated by the calculation of net tax losses from a brain drain in the Republic of Serbia). As a result of this, we recommend the development of a methodology for assessing tax losses from brain drain, taking into account the best practice of BEPS Action 11,[31] the use of which could reliably indicate the extent of the problem in the context of jurisdictions. Such a methodology would consider both the direct effects, such as losses of tax revenues in the donor country and their gains in the recipient country, and indirect effects, such as benefits from remittances to members of emigrants' families, transfer of knowledge, etc.

4.2.3. Disclosure of the Tax Burden on Certain Individuals (Action 12)

The authors of the BEPS Plan note: "the lack of timely, comprehensive and relevant information on aggressive tax planning strategies is one of the main challenges faced by tax authorities worldwide" (OECD 2015d, 9). As a result, in order to obtain preventive information, the OECD recommends the development of a set of mandatory rules for the disclosure of information regarding aggressive transactions, taking into account the balance of business and government interests. According to the OECD, the implementation of a tax disclosure mechanism may

[29] *Ibid.*

[30] *Ibid.*

[31] For example, the OECD report on Action 11 of the BEPS Plan provides the possibility of applying six indicators when assessing the extent of tax base erosion. It is also noted that the indicators developed are illustrative because of possible limitations in data availability. Therefore, in our opinion, even the use of the methodology outlined in the first part of the article would make it possible to understand the preliminary scale of tax losses from brain drain.

pursue the simultaneous achievement of the two goals. First, such an instrument allows competent authorities to more effectively respond to changes in tax behavior of the taxpayers, second, it acts as a strong deterrence tool – both taxpayers and promoters of schemes will be more careful in choosing one tax scheme or another, if there is a requirement to disclose it (OECD 2015d, 9). Despite the fact that Action 12 is not included in the so-called BEPS minimum standards, some experts suggest its acknowledgement as a next BEPS minimum standard (Mosquera Valderrama 2018). Moreover, it should be noted that the ideas of BEPS 12 are actively being implemented[32] (Directive 2018/822/EU), however, these changes have far from a positive perception by business representatives (EY 2018b).

So, in our opinion, the basic ideas of the BEPS Action 12 can be applied to cases of brain drain. For example, companies could provide information to the tax authorities about employees:

1) who recently moved to work in this country;
2) who could potentially be a tax resident of another state (other states);
3) whose level of tax burden is zero or close to it;
4) whose place of physical location during the performance of employment duties does not coincide with the place of payment of employment income.

In the future, such aggregated data could be included in the scope of the information exchange and form the basis for calculating tax revenue losses. However, it should be noted that the OECD indicates that the "lack of clarity and certainty can lead to inadvertent failure to disclose, which may increase resistance to such rules from taxpayers" or "could result in a tax administration receiving poor quality or irrelevant information" (OECD 2015d, 19). That is why such tax policy measure, if implemented, should be thoroughly designed.

4.2.4. Digitalization of the Mutual Agreement Procedure (Action 14)

Data from the OECD jurisdiction-specific guidance (OECD 2019a) indicates that today subjective criteria are already used by many jurisdictions in determining the tax residence of individuals. This trend will probably continue to grow, since the presence of only objective criteria in the tax legislation does not reflect the tax nexus of an individual with a country properly. A possible overlap of subjective criteria in

[32] See: Council Directive (EU) 2018/822 of 25 May 2018 amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements

different states inevitably can lead to an increase in the number of cross-border tax disputes.

Almost all double tax agreements contain rules related to the mutual agreement procedure. For example, Article 25 of the OECD MC provides for a mechanism, independent of the usual legal remedies available in domestic law, by which the competent authorities of the Contracting States can resolve disagreements or difficulties related to the interpretation or application of the Convention on a mutually agreed basis. However, as noted by the OECD itself, despite the widespread dissemination of this provision in double tax treaties, the current mutual agreement procedure is still far from ideal and requires reform.[33]

The BEPS Action 14 recommendations were aimed at solving some of the mentioned problems but in our opinion it does not contain revolutionary ideas; therefore, a detailed disclosure of the essence of BEPS Action 14 is not the purpose of this article. We applaud the positive developments of the MAP mechanism after the implementation of BEPS Action 14; according to the OECD, as of 2017, the average term for solving tax disputes under the MAP is 30 months, for cases related to transfer pricing, and 17 months for other cases.[34] However, we consider these terms "luxurious" for modern international taxation.

In our opinion, it is time for a "real-time" mutual agreement procedure that would reduce the level of transaction costs and time costs for all parties. Moreover, speeding up the MAP process can lead to more rapid accumulation of the MAP experience that states can use to improve their brain drain policies. As a result, we recommend the development of a digital mutual agreement procedure for competent authorities, whose presence would solve the issues of a multiple residence of "drain brains" in "a few clicks".

4.2.5. Multilateral Instrument (Action 15)

In July 2018, the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (Multilateral Instrument or MLI) was signed by more than 85 jurisdictions. This multilateral agreement is the "new word" in international taxation, as it allowed a large number of changes to be introduced in double tax treaties in a synchronized manner, without the need for separate negotiations for each of the double tax treaties.[35] We believe that this experience can be

[33] See: OECD. Action 14 Mutual Agreement Procedure. *http://www.oecd.org/tax/beps/beps-actions/action14/* (last visited 25 September 2019).

[34] See: OECD. Mutual Agreement Procedure Statistics for 2018. *https://www.oecd.org/tax/dispute/mutual-agreement-procedure-statistics.htm* (last visited 25 September 2019).

[35] See: OECD. Action 15 Multilateral Instrument, *http://www.oecd.org/tax/beps/beps-actions/action15/* (last visited 25 September 2019).

useful in a coordinated fight against brain drain. Among the priority issues requiring the development of a "single view" in the context of improving the function of double tax treaties, the following can be distinguished:

– Does the current version of the preamble set out in the current versions of the OECD and the UN model conventions (OECD 2017a; United Nations 2017) require clarification that the bilateral tax agreement does not apply in situations leading to "aggressive" attracting of "brains"?
– Does the current version of Article 15 of the OECD and UN MCs related to income from employment reflect the economic nature of such income in cross-border situations?
– Is a separate article related to cross-border taxation of scientists, professors, etc. necessary in the subsequent versions of the OECD and the UN model conventions?
– Does the current version of the Article 14 of the UN MC, about income from independent professional services, need an update?
– Are the provisions of the Article 17 of the OECD and UN MCs, related to income of sportspersons and entertainers, in line with the economic nature of the value creation in this area in the era of digitalization?

4.2.6. Value Creation in the Context of Brain Drain (Actions 1, 8–10, 13)

The current distributive rules and nexus rules that are present in the double tax treaties and domestic legislation based on the concepts of source, residence, place of physical employment and others, discussed in the analysis presented in section 3 above, do not reflect the value creation process of the "talent creating, developing and exploiting". "Talents" can potentially create value for their employers and society at large and can earn high income for themselves. However, "talents" do not come from nowhere; it takes time and effort, nurture, training and education in order to create the "initial talent", which is developed by the different kinds of collaborations and activity. So, if we apply the value-creation approach that is proposed in BEPS Project Actions 8–10 (OECD 2015a*)* to individuals, we can argue that countries where significant contributions to "talent creation" were made can have potential subsequent rights to tax such an individual's incomes. This line of argument can potentially be reflected in the OECD MC and the UN MC, in order to ensure fairness of sharing the global tax pie consisting of the incomes of such talented individuals. Such a substantial form of nexus may seem complicated, however, in practice it can be a useful proxy for income allocation of

highly-skilled workers in the global digitalized and mobile world, where value is increasingly created by intangible assets. Below we offer some conceptual ideas for such an approach.

First, the state where a person obtained their professional education and crucial experience can potentially be regarded as a state which has a right to tax at least some part of the subsequent income of such a person, especially in cases where education was government– funded. This idea can also be developed for the case of sportspersons leaving the state where they were trained and took their first steps in professional sports. Another relevant case is if the researcher who invented a new technology in a given state, based on the research infrastructure in that state, plans to move to a different state for the monetization of his invention. Generally, this idea is just a projection of the approach described in the OECD International Transfer Pricing Guidelines regarding corporate restructurings (OECD 2017b). The basis for such an idea is the result of the analysis, supporting the ease with which the donor state can lose taxing rights for talents in the case of IT specialists, sportspersons and academics, mentioned above.

Second, in determining the place of taxation of the talent's income that was generated distantly by the means of telecommunication or electronic networks, we suggest the allocation of part of the tax base to the county where the economic source of such income is situated – which can be the country of the market audience watching the online broadcast or the country of the employer who pays to the distant IT specialist. This idea is in line with the OECD work on the digitalization of the economy (OECD 2019b).

Third, the approach developed in BEPS Action 13 (OECD 2015e) for developing harmonized global rules of reporting information summarizing the activities of a multinational corporation in all the states where it is present can also be quite useful as an administrative tool, forming basic tax risk assessments for highly mobile individuals. In the same manner as in the case of the country-by-country reporting by Action 13 of the BEPS Project, such an approach can start with the application only in regard to the global economic activities of individuals with a global income exceeding a defined, relatively high threshold. This administrative requirement is critical in the case of taxing the income of the celebrities, including sportspersons and entertainers, but could in the future also be used as the basis for assessment of the income of the "digital nomads".

5. CONCLUSION

The main results of the analysis above are outlined below.

1) The domestic tax residence rules of donor countries of qualified specialists make it quite easy to break the personal nexus with the tax jurisdiction of the countries of emigration, which leads to their unfair loss of tax revenues. So, if countries don't want to lose tax revenues they should introduce more strict criteria for tax residence status, as well as special rules aimed at creating tax obstacles for termination of tax residence in the country, such as exit taxes. They should also consider this policy when negotiating tax treaties, which usually limits their rights to taxation of both the migrating and the offshoring workforce.

2) The rules for eliminating double taxation provided by both the OECD and the UN model conventions are obsolete and do not reflect the current problems of distribution of taxing rights in the context of the analyzed talent migration strategies. Situations of double taxation, double non-taxation and unfair limitations of taxation rights of the donor states can arise as a result of application of double tax treaties. This problem is exacerbated in the context of several current trends, which include:

- development of digital marketing strategies for the promotion and distribution of entertainment content, for example, broadcasting sports events over the internet,
- increasing level of mobility of the skilled workforce, as well as expanding opportunities for working remotely, for example, in regard to IT specialists.

3) As for income of the mobile scientific researchers the provisions of the double tax treaties, based on relevant Articles of the OECD and the UN model conventions,[36] can lead to unsatisfactory results: unfair loss by the donor country of the right to tax the income of emigrating researchers and possible double taxation of their income, fragmentation and complexity of regulation.

4) In our opinion, a new tax policy ideology is needed for rethinking the global tax architecture, in the context of brain drain issue, which should be based on two general ideas:

(1) prevention of the migration of talents obtaining tax benefits, whose incomes are subject to double non-taxation due to the application of a combination of international and national tax rules,

[36] For example, Article 14, 15 and 20 of the UN MC (2017), Article 15 of the OECD MC (2017)

(2) compensation the unfair loss of tax revenues to the countries which educated and then donated their qualified specialists to other countries.

We believe that the positive experience of the BEPS Project can be transferred to a cooperative approach in addressing the negative tax implications of brain drain. The main objective of such a project would be to reform the existing architecture of international taxation in the context of increasing mobility of qualified specialists and taking into account the interests of developing countries, including, in particular:

- the permissible limits of tax policy in attracting talented migrants to one's jurisdiction,
- approaches to cooperation in administrative matters in this area,
- approaches to developing a methodology for determining the place of creation of added value by skilled migrants, which would be a prerequisite for the country to have the right to tax income created by their activities;
- streamlining the mutual agreement procedure in regard to cases of mobile individuals.

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BRAIN DRAIN: THE IMPACT ON TAXATION AND MEASURES TO COMBAT THE BRAIN DRAIN

During the debt crisis the number of highly specialized Greek scientists who had migrated abroad surpassed 250,000. The reasons that led to this result include the mismatch of supply and demand for skilled human capital in Greece, the high rates of unemployment, as well as underemployment, and the increased in the tax burden and social security contributions. In order to tackle brain drain, a number of measures have been announced, focusing on reducing the individual income and corporate tax, lowering VAT rates and streamlining tax incentives for investors. Tax-related measures must take into account the new environment that has been shaped after the implementation of the OECD Base Erosion and Profit Shifting project. In addition to that, they also must respect the fundamental freedoms and general principles of European Union law in general.

Key words: *Bhagwati tax. – Free movement of workers. – Harmful tax practices. – Special economic zones. – Tax competition.*

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1. INTRODUCTION: THE PHENOMENON OF BRAIN DRAIN IN NUMBERS

According to a 2017 report by the European Commission, about 17 million people in the EU moved to another member of the community; 32% of them were up to 34 years old. Germany and Britain were the top destinations. The top countries of origin were Romania, Poland, Italy, and Portugal.

Similarly, according to Eurostat figures, during the debt crisis the number of highly specialized Greek scientists who migrated abroad almost doubled. This has resulted in more than 250,000 Greek scientists working abroad today. The figure corresponds to 12% of Greek university graduates, according to a May 2018 report by the General Secretary of Strategic and Private Investments. Of these, a vast majority are doctors and engineers, as demand in these sectors is huge, while job prospects at home are extremely limited. According to data from the Ministry of Economy and Development's Knowledge Bridges Platform (although, precisely because of freedom of movement, it is virtually impossible to accurately identify how many Greeks work in each EU country) it is clear that the largest number is concentrated in the United Kingdom, followed by the Netherlands, Germany, and Sweden.

According to the latest survey by ICAP People Solutions, 60% moved abroad after having already worked in Greece; 61% left Greece five or more years ago; moreover, over 50% between the ages of 30 and 40 years old, while 29% of Greeks abroad are 41 years or older. In 2015 the latter figure was just 12%. Today 48% of them are single. In 2015, the single persons amounted to 71%. According to the ICAP research, the brain drain population is growing older, living overseas, forming relationships, building a family. At the same time, it is evolving, taking up higher hierarchical positions, and earning more money. But the more that they achieve in their new homes, the more distant the prospect of returning to Greece begins to show.

The reasons that led to brain drain include the mismatch of supply and demand of skilled human capital due to the profile of the Greek economy, the high rates of unemployment as well as underemployment, part-time and related lower-skilled jobs due to the financial crisis, the political unrest, the perception of reduced meritocracy and increased corruption in the country, the general uncertainty, the prospects of personal and professional development abroad, the severe taxation and the enormous increase of social security contributions due to the measures adopted in Greece based to the economic adjustment programs.

2. FREE MOVEMENT OF WORKERS AND BRAIN DRAIN WITHIN THE EUROPEAN UNION

The free movement of workers is one of the fundamental rights enjoyed in the European Union by EU citizens. It is one of the four economic freedoms to which EU citizens are entitled, together with the free movement of goods, services and capital.

Article 45 of the Treaty on the Functioning of the European Union (TFEU) provides that the free movement of workers will be secured within the Union.

Free movement of workers entails the right to accept offers of employment actually made and to move freely within the territory of Member States for this purpose. It includes the right to stay in a Member State for the purpose of employment in accordance with the provisions governing the employment of nationals of that State laid down by law, regulation or administrative action and also to remain in the territory of a Member State after having been employed in that State, subject to conditions which is embodied in regulations drawn up by the Commission.[1]

This freedom of movement of workers within the EU has facilitated intra-EU labour mobility. However, in some regions ('sending regions') this freedom has led to a significant out-migration of their highly educated workforce to the advantage of other regions ('receiving regions'). This is determined by the growing competition for talent and the limited capacity of sending regions to create attractive conditions for these workers. Local and regional authorities (LRAs) in sending regions have to cope directly with the socio-economic effects caused by the significant loss of talent or brain drain. Addressing these effects may require the formulation of appropriate policies and/or measures to retain, attract, or regain a highly educated workforce.[2]

However, the free movement of workers has not only facilitated brain drain, it has also favoured related phenomena such as brain regain, which is the return to a region of the same high skills and/or competencies that were previously lost, and brain circulation, which is the continuous gain-loss of high skills and/or competencies.[3]

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[1] Article 45(3) TFEU.

[2] See the European Committee of the Regions, Commission for Social Policy, Education, Employment, Research and Culture (2018).

[3] *Ibid.*, 5.

3. THE IMPACT OF BRAIN DRAIN ON TAXATION

Academic literature has extensively studied the impact of the brain drain on the sending regions. It has been found that brain drain has a negative impact on the sending regions with severe fiscal consequences as it results in the reduction of taxable income and the unavoidable reduction of income tax as well as a decline in consumption, which also affects state revenue.[4] At the same time, however, a positive impact is also observed, as sending regions may also experience benefits with regards to brain drain such as return migration, remittances, incentives for investment in education and training and an improvement of governance.[5] Consequently, a country may experience a loss of tax revenue when the size of workforce shrinks. The labour market is also subject to other changes due to the emigration of highly skilled workers. In particular, when highly skilled workers migrate, the labour market shifts towards workers with lower skills. This in turn may result in an overall reduction of wages, which also affects tax revenue.

Indeed, income tax is closely linked to the constitutional principle of the ability to pay. This principle, enshrined in Article 4 of the Greek Constitution, is linked to the general principle of equality. According to the principle of ability to pay, each person shall contribute to the public revenues according to their capacity. The ability to pay principle imposes limitations on the burden of income taxation that a person can bear. Income tax cannot go beyond the minimum subsistence level; a taxpayer should be left with enough income after tax to provide for their basic needs. Therefore, as a result of the ability to pay principle, the lower the income of a taxpayer is, the lower their ability to pay is and consequently the lower the tax revenue for the state.

Similarly, the reduction of consumption, due to the lower level of income gained, may lead to a reduction of revenue from indirect taxes. Indirect taxes do not have the same limitations as income tax, as far as the ability to pay principle is concerned. Indeed, in the case of VAT, a mechanism of reduced rates for certain categories of goods is used to ensure that the basic needs of taxpayers are met and that they are not overburdened in an inflexible way. Nonetheless, consumption is directly linked to disposable income, i.e. income after tax: when disposable income is reduced, consumption is also negatively affected.

On the other hand, there is also a positive impact of brain drain on sending regions, even in terms of taxation. First of all, the spending power that might be reduced because of the brain drain, can be mitigated by the

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[4] *Ibid.*, 16.

[5] *Ibid.*

fact that workers that have migrated keep sending remittances back to their state of origin, therefore, at last partially, closing the created gap. However, remittances could also amplify the negative effect on tax revenues by negatively affecting the decisions to work, for instance by increasing the reservation wage, and de facto further reducing the tax basis. Another effect of emigration is that, as it mostly concerns working age population, the elderly left behind will increases the relative weight of pension and health spending on expenditure.[6]

4. TAX REASONS THAT MAY LEAD TO BRAIN DRAIN

From the diverse causes described, we will focus only on those related to taxation. The following interesting facts come from the OECD report Revenue Statistics 1965–2017.

1. In 2007–17, taxes in Greece increased by 8.2 percentage points of GDP, while in the memorandum years tax revenues increased from 32% to 39.4% of GDP. It is noted that although GDP was down 25% during the crisis, tax revenues totalled $ 95.9 billion in 2010, totalled $ 71.6 billion in 2015 and jumped to $ 78.9 billion in 2017. In fact, in the two years 2016–2017 Greece country was seventh in tax increases. In 2017 income and profit taxes amounted to 9% of the GDP and amounted to 22.8% of total government revenue.

2. Property taxes increased by 516%. In 2010, real estate taxes accounted for only 0.2% of GDP or close to € 600 million. Based on recent data, in 2017 taxes amounted to € 3.7 billion, i.e. 10 times the GDP percentage (2.1%). It should be noted that the situation is the same in Belgium, France and Luxembourg.

3. Greece has the lead also in the indirect taxes. Taxes on goods and services reached 15.4% of GDP in 2017, i.e. 39.1% of total taxes. A comparison with the Eurozone ‘big ones’ illustrates the huge differences: in Germany, indirect taxes accounted for 26.2% of revenue in 2018, 29.2% in Spain, 24.4% in France. Only Portugal exceeds Greece, with indirect taxes accounting for 39.8% of total tax revenue.

5. BRAIN DRAIN AND TAX COMPETITION BETWEEN COUNTRIES

Apparently brain drain affects the tax competition between countries, as they compete to offer a better tax environment in an attempt to reverse brain drain or to attract highly skilled workers (brain gain).

6 See Alcidi, Gros (2019).

Workers usually reside in the place (country) where they earn their income and pay taxes. Given differences in (pre-tax) wages, the decision to relocate then must take into account a package of national tax rates combined with local public goods (e.g. infrastructure and other amenities). This can then lead to beneficial competition among jurisdictions regarding the best package of taxes and local public goods.[7]

Overall, while the temptation to lower taxation on labour to prevent further shrinking of the tax base is strong, this may not work as other factors could be much more important when deciding about moving. Satisfaction with standards of living, including opportunities for children, may be much more relevant than a lower marginal tax rate on income. This could especially be the case for high-skilled workers.

Therefore tax competition for mobile labour should not be an important concern. It would anyway be at odds with the idea that the free movement of workers in the EU is a beneficial aspect of the single market and it also seems to contradict the idea that the movement of workers is a channel for absorbing country-specific shocks.[8]

6. MEASURES TO TACKLE BRAIN DRAIN

One of the first measures in order to tackle brain drain introduced by the previous government in Greece was instated on 31 December 2018. Specifically, the Greek parliament approved new provisions that specified the conditions for the application of Article 71D of the Income Tax Code (law 4172/2013), introducing a "super tax deduction" of the gross revenues for employers' social security contributions, for the creation of new full-time jobs[9].

More specifically, under the above provision, 150% of an employer's social security contributions for the creation of new full-time jobs are deductible from the gross revenues of legal persons and legal entities (including physical persons engaged in a business activity), up to a maximum of 14 times the minimum wage of an unmarried employee over 25 years of age, provided there is an increase of the average number of employees during the year, compared to the average number the previous year, and there is an increase of the total cost of employee wages during the year, compared to the previous year.

Furthermore, administrative decision No. 1244 provides that the tax incentive applies for the recruitment of young people up to 30 years

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[7] *Ibid*.

[8] *Ibid*.

[9] The incentive applies starting with the 2019 tax year.

old, at the date of recruitment, and long-term unemployed persons registered with the labour employment office (OAED), or other unemployment funds similar in operation to the OAED, at the time of their recruitment. The incentive also applies to the conversion of part-time or rotation contracts, and service or project-based contracts, into full-time employment contracts.

Finally, it is worth mentioning the measures adopted within the framework of the initiative "We Choose Greece – Building Bridges of Knowledge and Cooperation", which aims to help tackle the brain drain phenomenon abroad by 'connecting' all Greek scientists, no matter where in the world they are, by connecting them with Greece, for as long as they remain outside the country. In this context, after an evaluation of the proposals submitted by a special committee, prizes are awarded to transnational scientific-research cooperation networks, involving higher education degree holders[10] or business partnership proposals for the production of a specific product or service in Greece involving higher education holders[11], who are either of Greek or EU origin, or third country nationals who have residence in Greece under specific conditions. In order to ensure that the eligible persons actually receive the prize money, it is provided that the cash prizes cannot be confiscated, they are not subject to any kind of withholding tax and are not offset by any liabilities of the beneficiary to the Greek State[12].

The new Greek government, elected on July 2019, is planning "a comprehensive tax reform that will have a four-year horizon and will accelerate growth". The overhaul will focus on reducing income and corporation tax, cutting VAT, streamlining tax incentives for investors and abolishing emergency levies imposed during the Greek debt crisis to meet conditions set by bailout creditors. Starting 1 July 2020, the insurance contributions will start to decrease gradually. It will only be provided for full-time employees.

The recently voted Law 4621/2019, which was approved by the Greek parliament on 31 July 2019 (several days after the elections),

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[10] Specifically, those who are either of Greek or EU origin, or third country nationals who have had residence in Greece for at least three years, and who reside and work in the country they represent for at least one year at the time of application. Each network is represented by at least two (2) countries, one of which must be Greece.

[11] Specifically, those who are either of Greek origin or EU or third country nationals who have resided in Greece for at least one year three years, and who have resided and worked abroad for at least one year at the time of the application.

[12] Financing of the total amount of money distributed is financed by the national part of the Public Investment Program (PIP). The total amount of funding may not exceed three million euros per year. The total annual amount of aid is the budget of the number of projects in the Public Investment Program and is determined by decision of the Minister of Finance and Development.

significantly reduces the Annual Real Estate Ownership Tax (ENFIA) paid by individuals. The ENFIA, which is comprised of a main tax and a supplementary tax, is levied on real estate located in Greece, owned by legal entities and individuals. The new legislation also makes improvements to the instalment payment option for tax liabilities that was introduced in May 2019 (law 4611/2019).

Furthermore, the prime minister presented at the 84th Thessaloniki International Fair the main tax measures that his government intends to submit for a vote to Greek parliament, in order to promote economic growth in Greece and also deal with brain drain. He announced the reduction of the corporate income tax rate from 28% to 24%, the reduction from 10% to 5% of the withholding tax on dividends and the reduction of the lower income tax rate for individuals, for income up to 10.000 euros, from 22% to 9%. Furthermore, in order to promote the construction sector, he announced the introduction of a 40% discount on costs related to building renovations. In addition to the above tax incentive for building renovations, he announced the suspension of the payment of VAT on new buildings (for three more years) and the postponement of the imposition of capital tax on the transfer of real estate.

Finally, the prime minister announced further tax measures to be introduced in the next fiscal years, after 2020 and 2021, and specifically the abolishment of the business duty on entrepreneurs and self-employed, the introduction of an accelerated depreciation rate (up to 200%) for specific investments, the progressive reduction of the solidarity contribution on income that was introduced as an urgent measure during the economic crisis, and the income tax reduction on benefits in kind provided by companies to executives and employees, such as vehicles, etc.

The new tax measures announced by the Greek government intend to support the effort for growth and to deal with the brain drain. Lowering tax rates would help the Greek government to achieve the above goals, since higher tax rates influence people choices regarding the location of work and life and generally the mobility of young workers.

Furthermore, at the 84th Thessaloniki International Fair the prime minister announced the creation of a technology park that will host cutting-edge companies, free zones of commerce/free economic zones/ special economic zones (SEZs), which can be a model for other free zones of commerce in Greece, especially in some border areas that are very important because of competition to the north. Moreover, the government announced the simplification of the relative procedures specifically for industrial zones.

However, in the course of introducing such free zones of commerce, the Greek government should be cautious, since according to a new report

from the OECD and the European Union Intellectual Property Office, titled Trade in Counterfeit Goods and Free Trade Zones the illicit trafficking of products-monkey strengthens, unintentionally, the continuous growth of free trade zones, where economic activity is driven by reduced taxes and customs controls, less regulation and limited supervision. The report notes that exports of counterfeit and pirated products from a given country or economy increase with the number and size of the free trade zones it hosts.

The Greek government has not yet announced the details of these Special Economic Zones. In any case, the government should take into account the Base Erosion and Profit Shifting considerations in order to avoid generating harmful tax practices and competition. In this respect, it should adopt tax measures aimed at avoiding undesirable tax planning structures used by Special Economic Zones, and notably the requirement of substantial activity, controlled foreign company rules, etc. Also, the Greek government should not be overoptimistic, since in addition to tax incentives, other factors also influence the location of incorporation of the companies and corporate decision making in general. Such factors are political and economic stability, legal and tax certainty and transparency, availability of skilled labour, land policy, etc.

Furthermore, until now the Greek government has not introduced measures such as exemption from income tax for young people up to a certain age, which is the case with other countries, such as Croatia and Poland. In any case, analysts have strong doubts about whether such tax reliefs would reverse the brain drain of talented and educated youths to other countries that offer higher wages and other important job opportunities. According to them, tax exemptions, even full exemption, are probably not enough to tackle the brain drain. “They fail to address the root of the problem”, explains an Economist Intelligence Unit (EIU) analyst and warns that the flight will be intensified in the long run if there are no effective initiatives to stimulate growth and improve labour market conditions.

It is noted that, in addition to effectiveness considerations, the introduction of such measures, i.e. tax exemptions for young people, may pose issues regarding their conformity with the constitutional principle of tax equality.

If, however, lower tax rates or other tax incentives are not effective in reversing brain drain, can the same be considered responsible for causing brain drain? In 2017 Greece recorded the highest tax rates on labour in the European Union, reaching 43.3%, whereas Bulgaria recorded the lowest rates, at 24.3%.[13] There is concern that high tax rates might constitute an incentive for emigration, especially in the case of highly skilled persons.

[13] Alcidi, Gros, CEPS (2019), section 5.1.

However, up to now, there is limited evidence that mobile labour locates on the basis of tax reasons. This seems to be the case even if the semi-elasticity of migration appears higher for higher incomes and some countries had successful preferential tax treatment for high-earning foreigners.[14]

7. OTHER PROPOSALS TO TACKLE BRAIN DRAIN: THE EU LAW PERSPECTIVE

Literature has proposed that (usually temporary) restrictions on emigration be imposed on highly skilled or highly educated persons who have received educated at the public expense.[15] Such restrictions, however, on the free movement of workers, even temporary, are not compatible with the freedom of the movement of workers with in the EU, as protected by the TFEU, and therefore do not constitute a realistic proposal.

Another measure that has been proposed is the imposition of what is referred to as a 'Bhagwati tax' on emigrating skilled workers. A Bhagwati tax is, most generally, an 'exit tax' paid by a would-be emigrant with the intent of compensating their country of origin and for the training investment made in their skills.[16] Again, an exit tax that would constitute an obstacle to the free movement of workers within the EU would be very difficult to reconcile with the fundamental freedoms and therefore this measure would not be a viable proposal for addressing brain drain in the EU. The proposal of a form of tax credit would not entail such concerns.

Under this proposal, the receiving country, which is the country of residence of the highly skilled/educated worker, would take on the responsibility to assess the taxpayer with the tax due in their origin country, remit the tax so due to the origin country itself, and give an equivalent tax credit from the tax due in the worker's country of residence.[17] Within the EU there is a very high level of cooperation between tax authorities and this would make this proposal feasible and easy to implement. Such a measure, however, would require political consensus within the EU and with the states competing for tax revenue this seems rather far reaching at this stage of integration of the EU.

[14] *Ibid*.

[15] See the analysis in Lister (2017, 73 et seq., and n 4), who refers to the proposal by Gillian Brock, Prosperity in Developing Countries, the Effects Departing Individuals Have on Those Left Behind, and Some Policy Options, in *Debating Brain Drain: May Governments Restrict Emigration?*, edited by Gillian Brock and Michael Blake. 36, 37 (2015), aimed at protecting the workforce in developing countries.

[16] See the description and comments in Lister (2019, p. 79, n 26).

[17] See Lister, *ibid*. Lister has loosely based his proposal on the foreign tax credit that is available to US citizens living and working abroad.

8. CONCLUSION

The use of tax policy to address brain drain has been proposed by several authors, institutions and governments around the globe. In this regard, the proposed or introduced tax measures include the co-called 'Bhagwati tax', a form of exit tax, the use of tax credits, some of them modelled on the foreign tax credits US citizens receive in certain situations for taxes paid in other countries, tax incentives for the increase of investments, or even more the suppression of income tax or other tax reliefs for young people up to certain age (e.g. 25 or 30 years old).

Tax policy can contribute to the effort to address drain brain, and specific tax measures can be more efficient than others in stimulating growth in general. Nevertheless, it is strongly proposed that, having in mind fiscal considerations of course, to adopt a larger tax reform, with a reduction of the effective top/marginal rate and the adoption of tax incentives for businesses aimed at the recruitment of young workers, especially the highly skilled. But the brain regain cannot be resolved only by tax policy, but rather through large scale fiscal and social reform, which would deal with the causes of the drain brain phenomenon. Also, if we wish the Greek scientists who moved abroad to return in Greece, or at least to prevent others from making the same decision, we must eliminate the reasons that led them abroad, i.e. to change the country's economic growth pattern in order to match the supply and demand of skilled human capital in Greece.

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TAX MEASURES TO COMBAT BRAIN DRAIN: (IN) COMPATIBILITY ISSUES WITH DOUBLE TAX CONVENTIONS AND A POTENTIAL WAY FORWARD

This article analyzes the interaction between domestic tax legislation applied to avoid or combat a brain drain and the OECD and the UN model tax conventions, the two main models used by states in tax treaty negotiations. After it is demonstrated that brain drain taxes are incompatible with the current tax treaty network, the author presents alternatives that could be included in the model tax conventions, and consequently in tax treaties, to establish the compatibility of the measures, as well as a justification for the adoption of these alternatives in tax treaties involving developing countries.

Key words: *Brain drain. – Taxation of emigrants. – Tax treaties. – Right to development. – Tax benefits.*

1. INTRODUCTION

Since the migration of highly-skilled labor intensified after the Second World War, a discussion arose regarding the effects that such migration would have on the state of emigration. At first, it was thought that the emigration state would be worse off due to the emigration of highly-educated/highly-skilled citizens, so the term brain drain was coined in literature.[1] It was also argued that this process would have even

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[1] According to Dumitru (2012, 9 n. 3) the term *brain drain* was created in the 1960s by British tabloids to refer to the emigration of British scientists to the United States.

direr consequences in cases where the highly-skilled/educated individuals moved from a developing country to a developed country, so states and scholars started to analyze how to deter this occurrence or to at least compensate these less developed countries.

Amongst the ideas ventilated, there were proposals for the taxation of the emigrating persons by their former residence states (Bhagwati, Dellalfar 1972, 1–28; Bhagwati, Dellalfar 1973, 94–101) or for the establishment of restrictions on emigration.[2] Both ideas were met by considerable criticism. Regarding the establishment of a tax on emigrants, it was stated that the taxation would not be feasible and enforceable for developing countries (Oldman, Pomp 1975, 752), that the responsibility for the eventual adverse effects of migrations should not be on the emigrating person (Sager 2014, 573–576), that the migration is the consequence of a problem (Sampson 2013, 162–163) and that the migration can also be beneficial for the emigration state (McAusland, Kuhn 2006, 15–17; Agrawal, Kapur, McHale 2008, 1; Kumar 1967; Commander, Kangasniemi, Winters 2004; Hewitt 2007, 15–39). As for the restriction on the individual's emigration, it is argued that it is a morally questionable choice (Blake 2015, Part II). Ultimately, the proposals were never adopted on a wide scale,[3] albeit discussed in considerable detail at the academic level.

The increase in cross-border mobility since the 1990s has renewed the discussion, with an additional idea that states should not punish the individuals for deciding to emigrate; they should rather provide incentives for individuals to stay. Moreover, even though initially the issue had been framed mainly from the perspective of the less developed countries, more attention started being paid also to migrations between and within developed countries, with

legislators taking action to try to discourage migration of the highly-skilled/educated migrants to more developed regions of countries or to other developed countries.[4]

Despite the recent advances in the study of the topic, discussions are focused mainly on whether countries should be able to tax former

[2] According to Brock (2015, 73–74), states could establish that individuals that complete their studies, with or without a scholarship or loan, in a public or private university, must provide compulsory services to that state for a period of time.

[3] Bhagwati, Dellalfar (1972, 26) mention a tax applied by the Soviet Union on Soviet Jews who wished to emigrate to Israel, but by its characteristics it was an exit tax, not a tax like the one they proposed.

[4] On that issue see the recent tax exemption regime instituted by Poland as well as measures taken by states in the United States to provide tax benefits for graduates that remain in the state. The analysis from the perspective of developed countries is in line with the origin of the discussion during the brain drain of European scientists to the United States after the Second World War.

residents and how this can be done, with little regard to the consequences of potential taxation in the tax relations between states that have signed a convention to avoid the double taxation of income.[5] In that sense, it needs to be assessed whether the potential taxation prescribed in the domestic legislation of the emigrant's country would not be limited by a double tax convention signed by the emigration state. To do so, first it is necessary to define whether such taxes would be under the scope of the convention, the article that would be applicable, and the allocation rule in place. Furthermore, considering that the tax would fall under the scope of the convention and that the taxing rights of the emigration state would be limited, it is important to consider how such taxes could also be applied in a tax treaty situation.

This is the objective of this article, to assess whether the potential domestic prescription of the taxation of income earned abroad by immigrants who used to live in a country would be in line with double tax conventions based on the Organization for Economic Cooperation and Development (OECD) and United Nations (UN) model tax conventions. Moreover, in the event that such taxation is considered in contravention of the current international rules on avoiding double taxation, as prescribed by the model tax conventions, it will be discussed whether it is possible, and feasible, to reconcile these two systems, as well as how to perform this reconciliation.

Therefore, instead of focusing on whether countries should adopt tax measures to avoid brain drain or on analyzing measures that have already been adopted by specific states and their possible effects, this article will consider a scenario in which states have made the decision in their domestic legislation to either establish barriers for emigration, such as the imposition of a tax on future earnings, or to provide a beneficial tax treatment for individuals who decide to remain in their home states. From this starting point, the author will analyze whether these rules are in line with the current international framework of double tax conventions. After the (in)compatibility of the measures has been assessed, the author will look at the possible amendments that could be made to model tax conventions so that states that wish to enforce their domestic rules on curbing the brain drain are not restricted by international tax treaties.

2. THE BRAIN DRAIN CONUNDRUM

As mentioned above, this work will not focus on whether the levying of taxes on highly-skilled/educated individuals who have

[5] As notable exceptions in this matter, see Brauner (2010) and Stevenson (2016).

emigrated is the right manner in which to deal with brain drain or not;[6] whether it is better to provide positive reinforcements via tax breaks to individuals who remain or through any other eventual alternatives that exist for their emigration states. The assumption of this article is that the individuals' home state has already analyzed the best manner to deal with the brain drain, and that it is then necessary to verify whether the option adopted in the domestic legislation is in line with its model tax conventions. Before performing this analysis, it is crucial to understand the reasons why states see brain drain as an issue and want to avoid it or at least to guarantee taxing rights over the income of the emigrating person.

2.1 Emigration as a Problem: Brain Drain

One of the first reasons used to support methods to combat brain drain is that brain drain leads to a loss of revenue and welfare in developing countries (Bhagwati, Dellalfar 1972, 1–3; Bhagwati, Dellalfar 1973, 95; Brock 2015, 38). It is also argued that brain drain leads to a shortage of skilled labor in the emigration country (Lister 2017, 78) and this shortage can lead to further problems, especially in case of developing countries, where the number of highly-skilled/educated people is already scarce. It is also assumed that the emigration is a loss of the investment made by the developing country in the individual (Lister 2017, 78; Brauner 2010, 229), so this should be avoided. Furthermore, brain drain may be viewed as a subsidy from developing countries, which financed the education of the individuals, to the state to which the individual will emigrate (Freitas, Levatino, Pécoud 2012, 3; Altbach 2013, 42; Kuehn 2007, 1854), and may hamper the spillover effect and the development of institution-building assets, as studies have shown that higher educated people are more pro-democracy, so when they leave the country the local support for democracy may also diminish (Brock 2015, 40).

2.2 Emigration as Beneficial: Brain Gain/Brain Circulation

On the other hand, it is argued that the migration of highly skilled/educated individuals leads to a brain grain, with the circulation of knowledge, with diaspora effects (OECD 2008; Hewitt 2007, 15–39). Additionally, it is argued that the possibility of leaving provides incentives for individuals to acquire further skills, the income they send back is substantial, and if they return they might bring with them progressive ideas and enhanced human capital (Brock 2015, 40–41; Patterson 2007, 12; McAusland, Kuhn 2006, 19–20; Haupt, Janeba 2004, 21; Agrawal, Kapur, McHale 2008, 1–4). It is also said that countries export citizens,

[6] For a better understanding of some of the factors that might contribute to the brain drain in developing countries, see Docquier, Lohest, Marfouk (2007).

just like they export goods, and the idea of a loss assumes that the brain would be used at home, which is not always the case (Kumar 1967, 2079).

If it is believed that in the long-term the emigration fosters the development of the emigration state, countries should be drafting legislation to further incentivize the emigration of highly-skilled/educated individuals. However, despite this new line of research, it is still assumed that the probability of a brain drain is more likely (Lien, Wang 2005, 160), so discussions focus on what developing countries can do to restrict or limit this emigration.

2.3. Possible responses to Brain Drain

Based on the assumption that brain drain has a negative impact on a country's economy, proposals have been made on measures that could be adopted to curb this phenomenon. These proposals make use of the tax system in different manners, increasing the cost of a person's move by levying a tax or by providing incentives for the individual to stay in their residence state, and these possibilities will be studied below.

3. TAXES AS A BRAIN DRAIN DETERRENCE

One of the most prominent proposals on how countries should deal with brain drain is the Bhagwati tax, proposed in the 1970s by Jagdish Bhagwati. According to Bhagwati's original proposal, emigrants should have to pay a tax in their new residence state, to compensate the losses of the emigration states. This tax, which was viewed as payment to the developing country for allowing the individual to move abroad, would also reduce the incentive for individuals to move abroad (Bhagwati, Dellalfar 1973, 95).[7]

According to Bhagwati, the tax should be levied after immigration, on the income effectively earned, as opposed to prior to the emigration on expected income, and the tax should be collected by the developed country that received the emigrant.[8] The tax would be a surcharge, in the sense that emigrants would then be subject to a higher tax liability than other residents of this state. Bhagwati favored the idea that the collection should occur during the whole life of the emigrant, but since this would most likely not be accepted by the developed countries, he proposed that

[7] When analyzing the Bhagwati tax, John Douglas Wilson stated that such tax is desirable and that it could be a voluntary tax (Wilson 2011; Wilson 2008; Wilson 2005). Furthermore, it is argued that a brain drain tax can increase the welfare of the remaining residents (Scalera 2012, 447–467).

[8] Later, recognizing the issues with the collection by developed countries, Bhagwati focused on the tax being collected by developing countries.

the developing countries should be able to tax their former citizens for up to 10 years after emigration (Bhagwati, Dellalfar 1973, 96).

Regarding eventual obstacles to the collection, in the domestic legislation of developed countries, Bhagwati argued that the laws could be changed to accommodate this taxation. Also, he argued that the administration of the money and transfer to the developing countries should be done by the United Nations (Bhagwati, Dellalfar 1973, 95–96).

The proposal has been subject to considerable critics and a tax like the one proposed by Bhagwati has not been widely implemented, despite some of its characteristics being similar to those of an exit tax.

3.1. Brain Drain Taxes and the Model Tax Conventions

Now that we have briefly explained the issue of brain drain/gain and the proposal to limit (by means of income tax) the alleged losses that states suffer when skilled individuals emigrate, it is time to assess whether this tax would be in line with the OECD and the UN model tax conventions on double taxation and the double tax treaties using these models as a reference.

As the brain drain/gain issue focuses on the migration of individuals, in this analysis we will take a closer look at the taxation of individuals in model tax conventions, whether running their own business or working as an employee. Thus, in this section we will assess the compatibility of taxes such as the Bhagwati tax in light of articles 7, 15 and 21 of the OECD and the UN model tax conventions, as well as former Article 14 of the OECD Model Tax Convention and articles 12A and 14 of the UN Model Tax Convention. Articles concerning the receipt of passive income and the alienation of assets will not be covered, as the brain drain/gain debate focuses on the taxation of income that is earned by the emigrant when performing an economic activity. The provisions on pensions will not be dealt with for the same reason, while the article dealing with artistes and sportspersons is beyond the scope of this paper due to its special nature, which already modifies the treatment granted to entertainment activities when compared to other economic activities.

For that matter, we will consider the situation of John Doe, who emigrates from State A to State B, becoming a tax resident of the latter. The tie-breaker rule of Article 4(2) will be applied in the event that John Doe is also considered a tax resident of State A, according to this state's domestic rules.

3.1.1. Brain Drain Tax and its (In)Compatibility with the OECD Model Tax Convention

3.1.1.1. John Doe Earns Business Profits

The OECD Model Tax Convention prescribes, in Article 7, that profits from an enterprise of a contracting state[9] are taxed solely in that State, unless the enterprise carries on business in the other contracting state through a permanent establishment therein. The term business, as prescribed since the deletion of Article 14 in 2000, also includes the performance of personal services and of other independent activities.[10]

Analyzing John Doe's situation considering Article 7, it becomes clear that the profits that he makes by providing services, for instance, as a doctor,[11] will be taxed only in his state of residence. The question then becomes where will John Doe be resident based on Article 4 of a double tax treaty based on the OECD Model Tax Convention.

If following emigration John Doe is a resident solely of State B, State A will not be able to tax any income earned by John Doe, unless he maintains a permanent establishment in his former state of residence and the profits are attributed to the permanent establishment. As the discussions on brain drain/gain focus on taxing the emigrating person on their worldwide income, irrespective of where it was earned, this possibility will not be analyzed in this paper. The focus is, ultimately, on the compatibility of a brain drain tax with the general rule of Article 7, taxation exclusively in the enterprise's state of residence.

Thus, it becomes clear that a domestic tax for emigrants on the income earned after they moved would generally not stand the compatibility test with Article 7, since the emigrant does not commonly maintain resident status in the emigration states.[12] So, in our example, based on Article 7, only State B would be entitled to tax the profits earned by John Doe after emigration; i.e. taxation of this income by State A,

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[9] The definitions of enterprise and enterprise of a contracting state are given n articles 3(1)(c) and 3(1)(d) of the 2017 OECD Model Tax Convention: "(...) c) the term 'enterprise' applies to the carrying on of any business; d) the terms 'enterprise of a contracting State' and 'enterprise of the other Contracting State' mean respectively an enterprise carried on by a resident of a Contracting State and an enterprise carried on by a resident of the other Contracting State".

[10] As expressed in Article 3(1)(h) of the 2017 OECD Model Tax Convention "(...) h) the term 'business' includes the performance of professional services and of other activities of an independent character".

[11] Doctors are one of the examples normally examined in regard to the brain drain debate, especially the cases of African doctors who emigrate (Kuehn 2007, 1853–1855; Patterson 2007, 9)

[12] In some states, such as Brazil, emigrant can declare that they are not a resident anymore even shortly before he leaves the country.

John Doe's former state of residence, would be restricted by the model conventions and double tax conventions that contain a similar provision on taxation of business profits.

The situation could be different if State A still considered John Doe a resident according to its own domestic law. In line with Article 4 of the OECD Model Tax Convention, John Doe could be viewed, for treaty purposes, as a dual resident taxpayer, and the recourse would have to be made based on the tie-breaker rule of Article 4(2). If John Doe were deemed to be a resident in State B, the situation would have the same outcome as the one explained above: he would not be considered a resident of State A for treaty purposes and this state would only be able to tax his income if this income were linked to a permanent establishment therein.

If, on the other hand, John Doe were deemed a resident in State A, then State A would be entitled to levy income tax on the income earned by John Doe after his emigration. Thus, in the case of a residence-residence conflict resolved in favor of the former residence state, a brain drain tax instituted by this state would not infringe the provisions of the double tax convention. On this matter, it is also important to stress that if John Doe were deemed to be a resident of one of the contracting states, the other state would not be able to claim residence taxing rights based on the second sentence of Article 4(1). This outcome would not be affected by Article 1(3), the savings clause introduced in the 2017 OECD Model Tax Convention, because for treaty purposes John Doe would no longer be a resident of the other state, despite still being a resident of this state for domestic law purposes.[13] A third possibility for a brain drain tax to be in line with a double tax treaty based on the OECD Model Tax Convention would be if the tiebreaker rule did not resolve the residence-residence conflict of the individual, so both states would still be viewed, for treaty purposes, as John Doe's residence state.

Therefore, it remains clear that a brain drain tax can be in line with a tax treaty only in extremely limited situations, i.e. if a residence-residence conflict were resolved in favor of the emigration state or if the residence-residence conflict were not resolved and, as a result, the former resident was still considered, also for treaty purposes, a resident of the emigration state.

Naturally, this domestic brain drain tax could also be applied in cases where the states have not signed a double tax convention, but this does not affect the discussion on the compatibility of a brain drain tax with the model tax conventions and the double tax treaties based on them. Consequently, it can be affirmed that even if a brain drain tax were established by the domestic legislation, it would ultimately be applied in

[13] OECD, 2017 Model Tax Convention, Commentaries on Article 1, para. 21.

restricted situations, residence conflicts where the emigration state is considered John Doe's residence state, unresolved residence-residence conflict situations, and non-treaty situations. Even if it is considered that developing countries are, with a few exceptions,[14] conservative in the signing tax treaties, having a more modest tax treaty network, these cases still seem more an exception than the rule.

On that matter, despite the arguments that can be put forward in favor of the taxation of brain drain, and the fact that such taxation could occur only for a short period of one's lifetime, it remains clear that such taxation, except on the specific cases mentioned above, would be a clear violation of a treaty obligation, and that an eventual valid reasoning for a tax cannot supersede the express wording of a legal obligation as the one assumed under a double tax treaty.

It is interesting to note that in the original proposal Bhagwati suggested that the taxes should be collected by the developed country, but this idea was criticized based on eventual restrictions that the domestic laws of these states might establish on the tax collection on behalf of a foreign tax authority. Although the criticism is valid, as domestic legislations can indeed hamper the intended tax collection, it are incomplete, as the states' international obligations are not considered. As a matter of fact, such structure is the only one in line with Article 7 of the OECD Model Tax Convention since its inception in 1963, if considered that the residence state of the person for treaty purposes is the state to which they emigrated.

Nonetheless, it should be added that even if taxation is done by the developed country, complying in this sense with the wording of Article 7, such taxation could still run foul to treaty obligations, especially if the tax is levied as a surcharge, as originally proposed by Bhagwati. Such a surcharge tax would be in direct conflict with the non-discrimination provision of Article 24(1), because in that case State B would be taxing nationals of State A who are residents in the former, thus in the same circumstance as its own residents, in a more burdensome manner.

Ultimately, the establishment of a brain drain tax based on the proposals made since the 1970s would not produce any effects in treaty situations in which emigrants are carrying on their business as entrepreneurs in the developed country, as such taxation is not allowed based on Article 7 of the OECD Model Tax Convention and double tax treaties modeled after this provision.

3.1.1.2. John Doe Earns Income from Independent Personal Services

If the double tax treaty between State A and State B did not contain provisions on the taxation of income from independent personal services;

[14] e.g. India, which has a broad tax treaty network.

complying with the 2000 OECD Model Tax Convention, this income would be taxed under the scope of Article 7. Hence, the outcome would be the same as prescribed in the previous section, i.e. the treaty restriction on the taxation of income by the emigration state. Nonetheless, one may wonder whether this outcome would be different in treaties that still contain former Article 14 of the OECD Model, such as most treaties signed by developing countries. On that matter, it is important to note that the outcome would not be affected by former Article 14 of the OECD Model Tax Convention.

As expressed by the OECD when arguing for the removal of the provision, it is unclear whether there were any differences between the concepts of permanent establishment and fixed base (OECD 2000). And even if it is argued that the fixed base concept is broader, allowing for the easier establishment of a fixed base when compared with the permanent establishment, this eventual difference would have no bearing on the current situation, as State A is not intending to exercise taxing rights as a source state, but rather as a residence state, based on the fact that the highly educated/skilled individual emigrated.

In the case of John Doe, the emigration state would only be able to assert taxing rights via a brain drain tax if it was deemed to be, for treaty purposes, the residence state of John Doe. On that matter, the possibility for a brain drain tax to be compatible with a double tax convention would be, once again, the situation of a residence-residence conflict resolved in favor of the emigration state or an unresolved residence-residence in which the individual remained, also for treaty purposes, a resident of the emigration state.[15] Hence, the prohibition of brain drain taxation also holds true for double tax conventions containing former Article 14 of the OECD Model Tax Convention.

3.1.1.3. John Doe Earns Income from Employment

The discussions on brain drain usually focus on this specific situation, in which the emigrant is hired by a foreign employer to carry out his activities in a dependent manner, i.e. as an employee of the company. Despite the prevalence of this view, there has hardly been any consistent analysis of the compatibility of the brain drain taxation and Article 15 of the 2017 OECD Model Tax Convention.

According to Article 15, remuneration derived by a resident of a contracting state related to employment is taxable only in that state, unless the employment is exercised in the other contracting state. In that sense, similar to Article 7, the Convention recognizes the primacy of the residence state of the person to levy a tax on their income, unless the

[15] The latter possibility is further clarified by recourse to Article 1(3) introduced in the 2017 Update to the OECD Model Tax Convention.

person is present in the source for a considerable amount of time (more than 183 days) or their employer is a resident in the source state, or the remuneration is borne by a PE in the source state.[16]

The wording of the provision is clear, therefore there is no possibility to construe a theory in which the emigration state, the former residence state of the emigrant, would have taxing rights over the income from employment earned after emigration, unless the employment activities were being conducted therein. In the commentaries there is also no mention of such interpretation by any state, corroborating the idea that apart from the pleas in academic literature for the taxation of brain drain, the issue has not been thoroughly considered by the countries themselves. The situation would naturally be different if the emigration state was, for treaty purposes, still the residence state of the emigrating person, since in that situation Article 15, which focuses on taxation by the residence state of the income earner, would allow for the taxation of the person in the emigration state.

Hence, like the situation involving the potential taxation of business profits and income from independent personal services earned after emigration, the taxation of the income from employment earned after emigration is also not in line with the OECD Model Tax Convention, save in the specific situations already mentioned (residence-residence conflict resolved in favor of emigration state or unresolved conflict which allows the emigration state to still be seen, for treaty matters, as the emigrant's state of residence). Thus, a brain drain tax levied on income earned by John Doe after emigration would have limited applicability in tax treaty situations.

3.1.1.4. John Doe Earns "Other Income"

In cases where the income earned by the emigrating person does not fall under the scope of more specific provisions, such as the ones dealing with the taxation of business profits, independent personal services and employment, it will fall under the scope of Article 21, a catch all clause that also focuses on allocating taxing rights, in an exclusive manner, to the state of residence of the income earner, save in case where the income is earned through a permanent establishment located in the source state.[17]

Thus, in the case of John Doe, just as it happens when the income is under the scope of articles 7, 14 or 15, unless he was considered, for treaty purposes, as a resident of the emigration state, this state would not be able to levy a brain drain tax on the income he earned after emigration.

[16] OECD, 2017 Model Tax Convention, Article 15.

[17] OECD, 2017 OECD Model Tax Convention, Article 21.

3.1.1.5. Concluding Remarks on Relation of Brain Drain Taxes and the OECD Model Tax Convention

Taking the aforementioned into consideration, it is clear that irrespective of the existence of a brain drain tax in a country's domestic legislation, this tax would only apply to really limited situations: (i) dual treaty residence with the tie-breaker rule deeming the taxpayer to be a resident solely of the emigration state; (ii) unresolved dual residence conflict, so the taxpayer is still viewed, also for treaty purposes, as a resident of the emigration state; and (iii) non-treaty situations.

It is worthwhile noting that any attempt to justify such taxation by reference to the taxation of unrealized capital gains, which is allegedly permitted by the double tax convention, as described in the commentaries on Article 13,[18] would be vague, as there is an important difference between these cases: while in the taxation of unrealized capital gains there is an actual profit which has been created in the residence state, although it was not yet monetized, in case of the brain drain taxation the tax base will only be created in the future, i.e. at the moment of emigration the taxpayer has not yet earned the income that the residence state wants to tax.

Therefore, it remains clear that the taxation of brain drain, as suggested by Bhagwati and subsequent authors, is not in line with the provisions of the OECD Model Tax Convention, save in very specific circumstances. This means that if the emigration state adopted these provisions in its double tax treaties, the establishment of a brain drain tax in domestic law will barely produce significant effects internationally, which naturally is not the desired result for the implementing country.

3.1.2. Brain Drain Tax and its (In)Compatibility with the UN Model Tax Convention

If, instead of adopting the OECD Model Tax Convention as the basis for its double tax treaties, the states base their negotiations on the UN Model Tax Convention, it remains to be seen whether the outcome would be similar to the one explained above, i.e. brain drain taxes would be severely restricted in face of the double tax treaties.

To reach a conclusion on the issue, we will analyze articles 7, 14 and 15 and 21 of the UN Model Tax Convention, as done in the case of the OECD Model Tax Convention, as well as recently-introduced Article 12A, which deals with the taxation of technical services, since the business carried out by the emigrating person could also fall under the scope of this provision.

[18] OECD, 2017 OECD Model Tax Convention, Commentaries on Article 13, paras. 8–10.

3.1.2.1. John Doe Earns Business Profits

Article 7 of the UN Model Tax Convention is based on Article 7 of the OECD Model Tax Convention, so it is not surprising that they adopt a similar position regarding the taxation of business profits, i.e. exclusive taxation in the residence state, save if there is a permanent establishment in the source state and the income was earned through a permanent establishment. However, expanding the possibilities for taxation at source, which is exactly the reason why the UN Model Tax Convention was created, Article 7 stipulates that if the income is linked to sales in the other state, of the same or similar goods or merchandise sold by the permanent establishment, or arises from business activities carried on in the other state that are similar to the activities carried out by the permanent establishment, the income will also be taxed at this other state.

Note that, similar to what occurred when analyzing Article 7 of the OECD Model Tax Convention, even though Article 7 of the UN Model Tax Convention would allow the developing country to tax a larger share of the income than Article 7 of the OECD Model Tax Convention, it would still not allow the emigration state to tax income earned by former residents after emigration. That is because the paradigm in international taxation always viewed the developing country as the source state, and the UN Model Tax Convention expands the taxing rights of source states.

In brain drain tax matters, taxation is not based on income being earned in the developing country, but rather by being earned by a person who decided to emigrate. Normally the source of the income will be on the immigration state, which would also be the person's residence state. Thus, as a rule, Article 7 of the UN Model Tax Convention does not allow for the levying of a brain drain tax. The sole exception to this rule occurs, as explained above, if the emigration state is still viewed as the residence state of the emigrating person for treaty purposes, be it by reference to the tiebreaker rule of Article 4(2) resolving the residence-residence conflict in favor of the emigration state or by the lack of a solution by this provision and the continuous view of the emigrating person as a resident, for treaty purposes, of the emigration state. As mentioned above, the latter is further clarified by the existence of a savings clause like Article 1(3) of the 2017 UN Model Tax Convention, which guarantees that the residence state of the individual is not limited on taxing its own residents, save in specific situations which do not include the one at hand, i.e. no solution for dual residence conflict. If this occurs, a brain drain tax would indeed be in line with Article 7 of the UN Model Tax Convention.

The issues concerning whether the new residence state or the former will levy the tax and eventual constitutional restraints to this levying is not affected by the choice for Article 7 of the UN Model Tax Convention, as this is a matter of domestic law. But as mentioned above,

the choice for taxation by the new residence state, which could then transfer the income to the former residence state, would comply with the wording of Article 7 if the new residence state is viewed as the residence state of the person for treaty purposes.

Therefore, in the case of John Doe, State A would still not be able to levy a domestic brain drain tax if State A and State B signed a double tax treaty in line with the UN Model Tax Convention, irrespective of the fact that the UN Model Tax Convention has broader taxing rights than the OECD Model Tax Convention

3.1.2.2. John Doe earns Income from Independent Personal Services

Differently from the OECD, the UN Model Convention maintained Article 14. Similar to the situation concerning Article 7, Article 14 focuses on income being taxed only in the residence state of the income earner, save if specific circumstances occur, i.e. the person has a fixed base regularly available in the other state or spends more than 183-days in such state. In that sense, the presence of the second test broadens the possibility of taxation of income at source when compared to the OECD Model Tax Convention.

The crux of the issue is indeed that this provision allows for taxation at source when economic activities are developed therein. In the case of a brain drain tax, which disregards the place where income was earned and focuses solely on the fact that the person emigrated from the state, Article 14 does not leave any leeway for the emigration state to tax the future income earned by the emigrant.

Hence, as has been a constant regarding the discussions of brain drain taxation and their interaction with double tax treaties, such provision only allows for brain drain taxation if the emigration state is, for treaty purposes, the residence state of the emigrant. As seen before in this article, this would only occur in case there was a residence-residence conflict that were resolved in favor of the emigration state or unsolved.

Considering that normally the emigrant will become a resident of the state which he moved and will have at least most of his personal or economic relations attached to this state, it remains clear that in only a handful of cases a brain drain tax would be allowed, with Article 14 generally restricting the taxation by the emigration state.

In the case of John Doe, if he ceases to be a resident of State A due to the emigration, this state loses the right to levy a tax on his income from independent personal services. But if for some reason he retains residence in State A while also establishing residence in a different state, it would be necessary to check the facts and circumstances to assess where he is a resident for tax treaty purposes. If he is deemed to be a resident of State B, State A would not be entitled to levy a brain drain tax

in treaty situations. On the contrary, if he is deemed to be a treaty resident of State A, either by application of the tiebreaker rule or if there is no decision on the matter so that he remains, for domestic law and treaty purposes, a resident of State A[19], the latter would be entitled to levy a brain drain tax over his income from independent personal services after emigration. Once again, it seems that such taxation would be the exception rather than a rule.

3.1.2.3. John Doe earns Income from Employment

Article 15 of the 2017 UN Model Tax Convention is an exact reproduction of Article 15 of the 2017 OECD Model Tax Convention, so the conclusions presented above are also valid at this point [20]. On that sense, taking the specific case of John Doe in consideration, income he earns after emigration shall be taxable solely in State B, save if the activities are done in State A for more than 183 days, or he is paid by an enterprise resident in State A or the payment is borne by a permanent established located in this state. In any case, taxation would occur because State A would be the source state of the income, not due to the levying of a brain drain tax.

As mentioned above, a brain drain tax would only be in line with the taxation of income from employment as prescribed in model tax conventions if State A is still viewed as the residence state of John Doe for treaty purposes. The possibilities of this happening are scarce, i.e. dual residence situation in which State A is still considered to be his residence state, be it because the tie-breaker rule decides in favor of this state or because the dual residence conflict is not resolved.

3.1.2.4. John Doe earns "Other Income"

Article 21 of the 2017 UN Model Tax Convention adopts the same general rule of Article 21 of the 2017 OECD Model Tax Convention, i.e. items of income not dealt with in the distributive rules shall be taxable only at the residence state of the income earner.[21] However, this provision expands on the approach adopted by the OECD, dealing on Article 21(2) also with independent personal services performed from a fixed base and adding a provision that allocates taxing rights to source states as regards income arising in that state.

Despite the broader prescription of source taxing rights, like the situation with Article 7 of the 2017 UN Model Tax Convention, Article 21 has no different bearing on matters of compatibility of brain drain

[19] The latter possibility is reinforced by the introduction of a provision such as Article 1(3) of the UN Model Tax Convention in the double tax treaty between the parties.

[20] See section 3.1.1.3.

[21] United Nations, 2017 UN Model Tax Convention, Article 21(1).

taxes with model tax conventions than Article 21 of the 2017 OECD Model Tax Convention. That is why, once again, the focus of the UN model tax convention is to grant more taxing rights to the source state, but in the case of brain drain taxes the states want to assert taxing rights over income earned by former residents, irrespective of where the income was sourced.

Therefore, to assess whether a brain drain tax would be in line with Article 21 of the 2017 UN Model Tax Convention, we need to ascertain where the emigrating person is a resident. In our example, if John Doe is a treaty resident of State A, Article 21 would determine that this state can tax the income earned abroad after emigrating. But if he is a treaty resident of State B, the levying of a brain drain tax in treaty situations would run foul to the international obligations assumed by the signing of the tax treaty. Once again, considering that John Doe moved to State B, the only chance for the levying of a brain drain tax by State A would be if there was a dual residence conflict resolved in favor of State A, or if there was no solution to the conflict and, as a result, John Doe would still be a resident of State A for treaty purposes.

3.1.2.5. John Doe Earns Income from Technical Services

While in the OECD Model Tax Convention technical services fall within the scope of the business profits article, since 2017 there has been a specific provision in the UN Model Tax Convention dealing with the issue. This provision answers the call of developing countries to detach the taxation of technical services from the permanent establishment concept.[22] In that matter, the article prescribes that fees for technical services arising in a state and paid to a resident of the other contracting state, may be taxed in the latter.[23] This is a rather unusual wording, as typically model tax conventions use the "may be taxed" formula to establish that the source state may tax.

To eliminate any controversy in regard to where fees for technical services arise, the article determines that fees for technical services arise in the state in which the payer of the fees is resident or in the state in which the payer of the fees has a permanent establishment or fixed base, and the fees are borne by this permanent establishment or fixed base.[24] This sourcing rule is complemented by another one which states that fees for technical services are not deemed to arise in a state in the case where the payer is a resident of that state, and carries on business in the other

[22] In practice some developing countries where already avoiding the need for the existence of a permanent establishment by inserting fees for technical services under the scope of the royalties article.

[23] United Nations, 2017 UN Model Tax Convention, Article 12A(1).

[24] United Nations, 2017 UN Model Tax Convention, Article 12A(5).

contracting state through a permanent establishment, or performs independent personal services through a fixed base, and the fees are borne by the permanent establishment or fixed base.[25]

The provision also clarifies that fees for technical services may be taxed in the contracting state in which they arise, but if the beneficial owner is a resident of the other contracting state the tax levied at the source state will not exceed a certain percentage of the gross amount of the fees paid.[26] The beneficial ownership concept is the also adopted on the articles on dividends, interest and royalties. Moreover, this provision establishes the relationship between Article 12A and other provisions of the 2017 UN Model Tax Convention. In that sense, it can be ascertained that in case of a potential conflict between Article 12A and Article 14, the former will apply if there is no fixed base in the source state, while the latter will apply if the income is linked to a fixed base in the source, as expressly provided on Article 12A(4).

The provisions of articles 8, 16 and 17, on the other hand, prevail over Article 12A, which means that even if the income from shipping, director's fees and remuneration of top level managerial officials, the earnings of artistes and sportspersons could be classified as fees for technical services, as defined on Article 12A(3), the rules prescribed on articles 8, 16 and 17 would apply, i.e. there would be no restriction for the taxation of the income at source, which is a different outcome than the one prescribed by Article 12A, which limits taxation to a percentage (to be agreed by the contracting parties) of the gross amount of the fees paid. If, however, the payments are not under the scope of articles 8, 16 and 17, Article 12A still determines the taxation of the income at source, albeit in a limited manner.

The article also provides a treaty definition of the term *fees for technical services*, stating that it entails any payment for services of a managerial, technical or consultancy nature, unless the payment is made: (i) to an employee of the payer; (ii) for teaching in or by an educational institution; or (iii) by an individual for services for the personal use of an individual.[27] Unfortunately, there is no definition of the terms managerial, technical or consultancy, with the commentaries recognizing that these terms may overlap.[28] On a positive note, the definition of fees for technical services does not make any mention of domestic law of states, which means that the provision intends to establish an autonomous definition of the term, which is a more beneficial approach to avoid conflicts of

[25] United Nations, 2017 UN Model Tax Convention, Article 12A(6).

[26] United Nations, 2017 UN Model Tax Convention, Article 12A(2).

[27] United Nations, 2017 UN Model Tax Convention, Article 12A(3).

[28] United Nations, 2017 UN Model Tax Convention, Commentaries on Article 12A, para. 67.

interpretation and subsequent recourse to the domestic law of states based on Article 3(2).

The shared allocation of taxing rights, with a limit on the amount to be taxed at source, is not applicable if the beneficial owner of the fees for technical services, while resident of a contracting state, does business in the other contracting state though a permanent establishment or performs independent personal services in the other state, through a fixed base, and the fees are effectively connected to the fixed base or permanent establishment, or with business activities of the same or similar kind as the ones carried through the permanent establishment or fixed base.[29] If this occurs the situation will fall under the scope of Article 7 (business profits) or Article 14 (independent personal services), following the regulation prescribed in these articles. As a shortcoming of this provision, one that can lead to considerable discussion between the states, there is no definition of the expression "effectively connected".

Finally, the article states that when, due to a special relationship between the payer and the beneficial owner of the fees or between both and another person, the amount paid as a fee for technical services is not at arm's length, the article applies only to the arm's length amount, with the excess part remaining taxable according to the laws of each contracting state and considering the provisions of the double tax treaty.[30] On that matter, the commentaries on the provision clarify that the expression "special relationship" covers not only situations of direct and indirect control, but also relationships by blood or marriage.[31] Moreover, it is important to stress that this is the same treatment granted on the articles regarding excessive royalties and excessive interest.

Applying these provisions to the case of John Doe, it can be said that after emigrating from State A he could be taxed on fees for technical services in the state in which the fees arise, i.e. where the payer of the services is a resident or where there is a permanent establishment or fixed base connected to the obligation to pay the fees and which bears the costs of the fees, or in his residence state. Considering this, as expressed above, brain drain taxes are not based on the idea of the business being developed in a state, but rather on the fact that they are earned by a former resident, it remains clear that the state does not intend to ascertain its taxing rights as a source state, reason why this possibility will not be analyzed in the present work.[32]

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[29] United Nations, 2017 UN Model Tax Convention, Article 12A(4).

[30] United Nations, 2017 UN Model Tax Convention, Article 12A(7).

[31] United Nations, 2017 UN Model Tax Convention, Commentaries on Article 12A, para. 130.

[32] It it important to note that if this were the case, State A, as the source state, would be able to levy a tax based on Article 12A.

Therefore, based on Article 12A, State A would only be able to levy a brain drain tax if it were still viewed as John Doe's residence state. As expressed on previous sections of this article, this would only happen if based on State A's and State B's domestic law John Doe is still viewed as a resident, according to the factors referred to in Article 4(1) of the double tax treaty between the states, and if the dual residence issue is subject to the tiebreaker rule, with the matter being resolved in favor of State A being the residence state, or if no decision was reached and John Doe is still viewed, for treaty purposes, as a resident of State A. In the latter case, if the treaty contains a provision like Article 1(3) of the 2017 UN Model Tax Convention it would be clear that State A would be entitled to levy its brain drain tax, but even if the provision were not present, this state would still be able to levy a brain drain tax, as the convention has not established any restriction on the domestic law taxation by State A as this state is still considered to John Doe's residence state.

3.1.2.6. Concluding Remarks on Relation of Brain Drain Taxes and the UN Model Tax Convention

Similar to the situation involving the OECD Model Tax Convention, as a rule, the signing of a double tax treaty based on the UN Model Tax Convention severely hampers the application of brain drain taxes. The differences between the OECD and the UN model tax conventions, with more taxing rights being attributed to source states in the latter, including the addition of a specific provision on fees for technical services, have no bearing on the discussion of the compatibility of brain drain taxes with double tax treaties.

This outcome is not surprising, since the focus of the UN Model Tax Convention is on allowing more taxation at the source and the discussion on brain drain taxes does not focus on taxation based on the source criterion, but rather on taxation by the emigration state. As the emigration state intends to exercise worldwide taxing rights over the income of individuals who have migrated, the only manner in which this can be achieved in a treaty situation is if the emigration state is still viewed, for treaty purposes, as the residence state of the emigrating person.

In the example above, regarding the taxation of John Doe by State A, this would mean that this state would still need to be considered John Doe's residence state to be able to levy a brain drain tax on him. For domestic law purposes that is not a problem, as the state itself determines who is viewed as a resident, but the issue is more complex when the states concerned have signed a double tax convention. This is because the tax treaty purports to determine the sole residence state of the individual,

and chances are that since John Doe has moved to State B and is currently living there, this state will also treat him as a resident under its domestic law, triggering a dual residence conflict. In that case, Article 4(2) would be applied to determine his treaty residence.

As it currently stands, Article 4(2) determines residence first based on where the individual has a permanent home. As John Doe emigrated from State A, chances are that he would only have a permanent home in State B, which would mean that the conflict would be resolved in favor of State B and the brain drain tax instituted by State A would not apply in the situation. If he maintains a permanent home in state A as well, it would be necessary to investigate his center of vital interests, where his personal and economic relations are. Once again, it is more likely that it would be in State B, but here it is possible that his center of vital interests, specially his personal relations, would still be in State A.

In case it was not possible to determine his center of vital interests, or if John Doe does not have a permanent home in either state, then the tiebreaker rule would determine that his residence state is where he has his habitual abode, i.e. where he is regularly. Once more it is more likely that the conflict would be resolved in favor of State B. If he has a habitual abode in both states or in neither of them, he would be deemed a resident only of the state of which he is a national. This is the first test which most likely will favor State A, although this is not certain. Ultimately, if he were a resident of both states or neither of them, states would have to solve the matter by recourse to a mutual agreement procedure. Therefore, as it can be seen, the chances are greater that John Doe would indeed be considered a treaty resident solely of State B, which would bar the levying of a brain drain tax by State A.

In a nutshell, by moving to State B, based on Article 4(1) John Doe would most likely be viewed solely as a resident of this state, which would mean that State A would not be allowed to levy a brain drain tax. Even if, for domestic law purposes, John Doe were still considered a resident of State A, the recourse to the tiebreaker rule of the double tax treaty between State A and State B would probably determine that John Doe is a resident of State B, with the result being, once again, that the levying of a brain drain tax by State A would not be in accordance with the double tax treaty.

If, on the other hand, John Doe were regarded as a resident of State A, the brain drain tax would be compatible with the double tax treaty. There are two possibilities for John Doe to be viewed as a resident of State A: (i) the analysis of the facts and circumstances of the case determine that he should be deemed a resident of State A, which, as demonstrated above, is not the most likely outcome; and (ii) the residence conflict is not solved by recourse to Article 4(2) and John Doe is still

considered a resident of State A and State B for domestic law and treaty purposes.

In the latter case, considering that, as demonstrated above, the articles of the conventions regarding business profits, independent personal services, employment income, fees for technical services and other income favor taxation by the residence state of the income earner, without establishing any restriction on taxation of these types of income by the residence state of the individual, State A would have no problem to levy its brain drain tax. This is corroborated by Article 1(3), the savings clause, recently introduced into the UN Model Tax Convention. But even if the double tax treaty between State A and State B does not contain such provision, State A would still be allowed to levy the brain drain tax, since the treaty would not prohibit such a tax.

Therefore, as it has been argued throughout this article, the possibilities for a brain drain tax to be compatible with double tax treaties are slim, and it cannot be considered that such tax would ultimately be widely used or generate significant revenue for the tax authorities of developing countries.

4. TAXES AS INCENTIVES TO AVOID BRAIN DRAIN

Apart from the institution of a brain drain tax, a state can also reduce the brain drain risk by adopting positive measures, ones that provide incentives for taxpayers to stay or to move to a country. In this section, we will study both possibilities and analyze whether they would be in line with the double tax conventions.

4.1. Taxes as Incentives to Retain Individuals

Just as taxes can act as a deterrent to the migration of individuals, they can also be used to provide individuals a better off situation, by means of credits or a reduced tax burden. One of the approaches is to discard the income tax levied on the population that might migrate, as done by Poland and studied further in another article of this journal, as well as by certain states in the United States, such as Mississippi.

In this sense, the government provides a tax exemption for certain categories of taxpayers, be it young taxpayers as in Poland and the United States, or individuals that earn a certain amount of income, if they remain living in the state. This is a trade-off in which the state ultimately ends up giving up on the tax income that could be collected in exchange for the maintenance of these individuals that are believed to help the state's economy of the state in the long term.

As regards the compatibility of such measures with the double tax conventions signed by states, there is no question that, considering that the benefit is granted to a resident of a contracting state, the situation would be under the scope of such convention as prescribed in Article 1(1) coupled with articles 2(1), 3(1)(a) and 4(1). Furthermore, the tax exemption would not infringe the double tax treaty, as treaties allocate taxing rights between states, they do not stipulate that a state is obliged to tax the income, irrespective of the type of income earned (business profits, independent personal services, employment income, other income). Moreover, it is worth noting that the articles studied above do not put any restriction on taxation by the residence state (apart from Article 23A and B, which prescribe an exemption or credit for taxes paid abroad).

If the resident individual only earned income in their residence state the situation would be even more clear-cut, as in that case this would be the sole state entitled to tax the income.

The fact that the state would not be restricted in its right to tax the resident individual does not mean that there would be no risk that the double tax treaties signed by the states could lead to questions on the tax treatment granted to these individuals. However, in that case the focus would not be on the distributive rules, but rather on the non-discrimination rule contained in Article 24(1). As provided on Article 24(1), "Nationals of a Contracting State shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith which is other or more burdensome than the taxation and connected requirements to which nationals of that other State in the same circumstances, in particular with respect to residence, are or may be subjected. This provision shall, notwithstanding the provisions of Article 1, also apply to persons who are not residents of one or both of the Contracting States."

Considering the example of John Doe, if instead of emigrating to State B he would remain a resident of State A and receive a tax exemption on his income, the nationals of State B that are residents in State A could request the same tax treatment of John Doe on the basis of Article 24(1) of the double tax treaty between State A and State B. Thus, to comply with its treaty obligations, State A might have to extend this beneficial tax treatment to all nationals of the states with which it has signed double tax treaties, leading to a greater loss of tax revenue, i.e. the measure might be counterproductive, since one of the concerns about brain drain was precisely the loss of tax revenue.

There is another issue that might arise in the establishment of preferential tax treatment for certain taxpayers as means to avoid brain drain: inequity in the domestic sphere, as usually benefits to avoid brain drain are granted to individuals who are already better off than the average resident. Despite the importance of this matter, we will not delve further

into its analysis since the focus of this paper is the compatibility of tax measures aimed at avoiding brain drain through double tax treaties, and this issue is a purely domestic one.

There is no issue regarding the compatibility of domestic tax exemptions with double tax treaties, as demonstrated above, save that the state that provides for the exemption might have, based on the non-discrimination clause normally contained in double tax treaties, to extend the exemption to nationals of all states with which it has signed double tax treaties. In that sense, it can already be ascertained that the provision of tax exemptions is a sounder approach to dealing with the brain drain than the institution of a brain drain tax, at least in regard to the state fulfilling its treaty obligations. Nonetheless, the adoption of a tax exemption and extension to all nationals of treaty partners resident in the state might be more detrimental to the state's finances than the restriction imposed by double tax treaties on the establishment of brain drain taxes, so states should consider this carefully.

4.2. Tax as Incentives to Attract Individuals

In addition to providing tax benefits for individuals who opt to remain in the state, it is also possible to offer a tax incentive to attract individuals to move to the state, an option which is becoming increasingly common. As an example of such a measure, the Netherlands has a 30% ruling for highly-skilled labor hired by Dutch employers.[33] According to this system, individuals who move to the Netherlands for their work and did not live within 150kms of the border for at least 16 out of the 24 months prior to moving, are entitled to a tax break on 30% of their income, i.e. 30% of the income will not be taxed for a period of 5 years, which can be renewed once.

Considering the example of John Doe, if such benefits were in place in State B, instead of being taxed by State A after his emigration or receiving a benefit to remain a resident of State A, he would receive a tax break granted by State B, as long as he moved to this state. Thus, once again, the issue would not be whether the emigration state could tax the income he earned after emigration, but rather whether State B "poaching" John Doe would be in line with the double tax treaties based on the OECD and the UN model tax conventions.

Like the incentives provided for individuals to stay in a country, tax breaks to attract individuals do not conflict with double tax treaty rules[34] as they merely determine that a state will give up taxing part of the income of certain individuals. In that sense, considering that the state

[33] Wet op de loonbelasting [Wage Tax Act] 1964.

[34] For more on the matter see section 4.1.

is not restricted by a double tax treaty in its taxing rights over this individual, it is still up to the state to determine in its domestic legislation whether the individual will effectively be taxed, so there is no conflict.[35] If the double tax treaty prescribes that only the other state can tax the individual, the tax break at hand would also be compatible (on the part that is exempt, as taxation of the remaining taxable income would indeed be restricted in such a situation), because it would also stipulate that no taxes would be levied on the individual.

This conclusion is in line with the fact that double tax treaties allocate taxable income, since it is still up to the person's residence state to determine how it will exercise its taxing rights, i.e. the double tax treaty does not stipulate the manner in which the income should be taxed, but only whether it may be taxed or not. The entire remaining taxation framework stems from domestic rules.

Nonetheless, like tax incentives to maintain individuals in a state, tax incentives to attract individuals may also need to be extended to nationals of a contracting state who decide to take up residence in the state providing the benefit, based on the non-discrimination clause of a double tax treaty (Article 24(1)). Additionally, this measure may generate discussions, from a domestic law perspective, regarding its equity.

The extension of the benefit to foreign nationals is not an issue per se, as these attraction systems, like the Dutch 30% ruling, do not consider the nationality of the person as a distinctive criterion for the receipt of the benefits. The issue concerning the equity of the system from a domestic law perspective, on the other hand, might generate considerable discussions, as the persons that can normally benefit from these attractions schemes are normally highly-skilled individuals, who already earn more than the average resident taxpayer. As mentioned in the previous section, this issue, although extremely important, is merely mentioned as a point of attention because it does not affect the compatibility of the scheme with double tax conventions, and is beyond the scope of this paper.

Overall, it is interesting that the provision of tax benefits is compatible with double tax treaties, but it does not resolve the problem that countries face when opting for a brain drain tax, i.e. it does not burb the loss of tax revenue. On the contrary, the provision of tax breaks for individuals who remain residents or who become residents may lead to an even higher loss of tax revenue than the one caused by the brain drain, as these breaks are also applied to persons who would already remain

[35] Although these measures do not conflict with tax treaties, one can question the behavior of developed countries that adopt such measures, as they can lead to the increasse in brain drain from other states, as argued by Assaf Razin (2017, 13–15). Altbach (2013, 41) is more contentious, stating that developed countries are robbing developing countries of their brains and this will significantly damage the latter.

residents or would move to the state, i.e. these persons' behavior is not affected by the tax break, as intended by the legislators, but they still benefit from the tax incentive.

Therefore, considering the revenue-collecting goal of the brain drain taxes, it is important to assess how these taxes can become compatible with double tax treaties.

5. ESTABLISHING THE COMPATIBILITY OF BRAIN DRAIN TAXES WITH DOUBLE TAX TREATIES

As it has been presented in this paper, the adoption of a brain drain tax presents a challenge to states that have signed double tax treaties, as such a tax cannot be applied in a treaty setting save in specific situations: (i) residence-residence conflict solved in favor of the emigration state, or (ii) unresolved residence-residence conflict. Furthermore, the network effect of tax treaties, normally seen as a positive trait (as it is generally accepted that the more tax treaties a country has signed, the better), leads to greater restriction on the adoption of a brain drain tax in a treaty situation, which is certainly not the idea that countries have when instating brain drain taxes. Thus, the question remains how to make brain drain taxes compatible with double tax treaties.

On that matter, the issue can be tackled by: (i) substituting the residence criterion with the citizenship criterion; (ii) amending the residence article; or (iii) modifying the treaties' distributive rules to allow the emigration state to tax future earnings of the emigrant.

5.1. Substituting the Residence Criterion with the Citizenship Criterion

As mentioned before, double tax treaties modeled after the OECD and the UN model tax conventions are applicable to persons who are residents of one or both contracting states, as prescribed by Article 1(1). In this sense, establishing the residence of the person becomes paramount in determining whether the person falls within the scope of the double tax treaty. A person that decides to emigrate will normally not remain a resident of the emigration state, and even if that occurs, the person will most likely also be a resident of the state to which they have moved and recourse to the tiebreaker rule would probably establish that, for treaty purposes, the person is a resident of the latter state. As a result, considering the distributive rules of the treaty, the emigration state would not be allowed to levy a brain drain tax on this individual.

Considering that a brain drain tax should apply also when the state has a double tax treaty in place, it would be possible to establish, like the

United States currently does, that the double tax treaty does not affect the taxation of its citizens by a contracting state.[36] The focus on the citizenship status of the individual, rather than only on the individual's residence, would solve any incompatibility between brain drain taxes and the tax convention at hand.

Although the adoption of citizenship-based taxation is possible, one should remind that currently the United States is the only country of the world that taxes on the basis of citizenship, so the adoption of this criterion would entail not only a significant amendment of double tax treaties but also of state's domestic legislation. Furthermore, there is a great risk that developing countries, which are believed to suffer more from the brain drain and would thus be more eager to establish a brain drain tax, would not be able to apply and enforce such a measure. The failed experience of the Philippines related to the adoption of a citizenship criterion for taxation shows that the solution may not be as straightforward as it seems.

Therefore, even though such an amendment would resolve the incompatibility issue between brain drain taxes and double tax treaties, it does not seem to be a feasible option for most states, especially the least developed ones that suffer greatly from brain drain and are in the weaker negotiating position when signing double tax treaties.

5.2. Amendments to the Residence Article

If the shift to taxation based on the citizenship criterion is considered unattainable or politically unfeasible, states still have the option of allowing for the establishing of brain drain taxes by means of amendments to the residence article of their tax treaties. On that matter, a sentence could be added to Article 4(1) determining that citizens are deemed to be perpetual residents of the state to which they are attached or that in case of emigration from one state to another the former would always be deemed to be the residence state of the emigrating person. Naturally, as an individual may live in various places during their lifetime it would be important to establish under what conditions the emigration state would still maintain taxing rights over the emigrating person, and it seems that combining such a rule with the citizenship criterion from the previous section may be a good solution.

Irrespective of which option is chosen, in both cases the amendment of the residence provision would guarantee that the emigration state would not run foul of its treaty obligations by establishing a brain drain tax.

Despite the potential desirability of such proposals, especially if it is considered that states should indeed levy brain drain taxes, it remains

[36] United States, United States Model Income Tax Convention, Article 1(4).

clear that they are still a considerable deviation from the current rules prescribed in the OECD and the UN model tax conventions, and that a similar outcome can be achieved by means of a less harsh change. Considering that brain drain taxes are not in line with double tax treaties because the emigration state is not the residence state of the emigrating person, at least for treaty purposes, and that as an exception these taxes are compatible with double tax treaties when a residence-residence conflict is solved in favor of the emigration state, the alignment of brain drain taxes to double tax treaties can be done by means of a reshuffling of the tie-breaker rules.[37]

As explained above, even in situations in which the emigration state is still viewed, for domestic law purposes, as the residence state of the emigrating individual, its taxing rights would be severely limited by double tax treaties because the tiebreaker rule would most likely be resolved in favor of the individual's new residence state. This is because the order in which the tiebreaker test is set focuses on the individual's physical link to a state (permanent home), economic and personal interests (center of vital interests), physical presence in the state (habitual abode), and ultimately the personal attachment of the individual to the state (nationality), thus the personal attachment to a state is only taken into consideration as a last resort.

However, if the tiebreaker rule were modified and the nationality test were the first criterion to be assessed, the changes that the emigration state would be able to tax its former resident would significantly increase. Note that differently from the switch to taxation based on citizenship or on deeming the emigration state as the perpetual residence of the individual, this would be a less troublesome change, as the nationality criteria is already present in the tie-breaker rule. This amendment would merely bring this criterion to the forefront of the residence-residence conflict for individuals, without establishing any different threshold for taxation. In the event that this criterion is not met, the remaining factors would still be assessed to determine where the individual is resident for treaty purposes.

5.3. New Distributive Rule in Case of Emigration

When analyzing the compatibility of a brain drain tax with the distributive rules of the OECD and the UN model tax conventions, more specifically articles 7, 12A, 14, 15 and 21, it became clear that all provisions allow for taxation of the income effectively earned by the person, giving preference to residence taxation of the income and, if certain conditions are met, allowing for source taxation too. However, a

[37] As suggested by Brauner (2010, 250), proposing to consider the individual's center of vital interests before the permanent home criterion.

brain drain tax would be levied on income earned after emigration, i.e. when the taxpayer is already a resident of another state. Consequently, based on the provisions of the model conventions, the emigration state would not have any taxing rights over this income, unless it was sourced therein.

If the option to align brain drain taxes with double tax treaties is chosen, it is necessary to modify the current structure of treaties and prescribe taxing rights to the emigration state over income that is earned after emigration. This could be achieved by adding a paragraph to each article stipulating a specific treatment for emigrating individuals, e.g. Article 7 would also prescribe that profits of an enterprise of an emigrating individual, whenever arising, may also be taxed in the emigration state, irrespective of whether the enterprise carries on business in the emigration state through a permanent establishment. Or a new article could be added to allocate taxing rights relating to emigrating individuals,[38] with emigration serving as the distinctive criterion for special tax treatment, in the same manner as income director's fees are dealt with in Article 16, and income from artistes and sportspersons in Article 17. The allocation rule would then prescribe that income earned by an emigrating individual may also be taxed by the emigration state.

6. JUSTIFICATION FOR THE AMENDMENT OF DOUBLE TAX TREATIES TO MAKE THEM COMPATIBLE WITH DOMESTIC BRAIN DRAIN TAXES

Having established the possible amendments that would make brain drain taxes compatible with double tax conventions, therefore fulfilling the objective of guaranteeing that in case the emigration state opted for a brain drain tax in its domestic law this tax would not be hindered by a double tax treaty, it is also necessary to consider how to justify these changes. As examined previously in this paper,[39] brain drain taxes are normally justified as a means to combat tax revenue losses stemming from the emigration of highly-skilled individuals. However, this is not enough per se to justify the redrafting of the allocation rules, as the same reason can be used by the individual's new residence state to argue that granting taxing rights to the emigration state is the equivalent of restricting their taxing rights over individuals that are residents in their states.

On that matter, considering that brain drain taxes are normally linked to developing countries, which are normally the ones that suffer

[38] As the 2017 UN Model Tax Convention has recently done regarding fees for technical services.

[39] See section 2.

considerably brain drain (Kuehn 2007, 1853–1855; Patterson 2007, 9), it can be argued that the amendments should be made in order to align the double tax treaties with the right to development (Souza de Man 2017; Silva 2009; Sengupta 2000).[40]

The right to development is a human right recognized by the United Nations as a right of individuals and states to participate in, contribute to and benefit from economic, social, cultural and political development.[41] Thus, it is recognized that states should have their right to development respected by other states (Souza de Man 2017, 25) and that more developed countries have the responsibility to support the development of their residents as well as residents of other states (Souza de Man 2017, 25). The Declaration on the Right to Development did not bind the states, not even the ones that adopted it,[42] so it might be argued that the right to development is not actually a right in the strict sense.

Nonetheless, since the Declaration on the Right to Development was adopted more than 30 years ago and that the United Nations has repeatedly stated that the right to development is a human right (UN, 2004, E/CN.4/Sub.2/2004/17; UN, 2001, E/CN.4/2001/WG.18/2 UN, 2000, A/RES/55/2;) with consensus being achieved in the Vienna Declaration and Programme of Action in 1993 (World Conference on Human Rights 1993), it can be argued that this right is already part of customary international law (Mansell, Scott 1994, 174; Villaroman 2001, 8; Have 2013, 3; Kunanayakam 2013, 48) and can indeed be counted on by developing countries in achieving their goal of development through the collecting of taxes (Souza de Man 2017, 31–32).

As a result, states could be considered to have the obligation to facilitate the development of all individuals and states, so developed country should assist developing countries. In fact, such assistance already exists by means of development aids, but this could also be done by allowing developing countries that are suffering brain drain to levy brain drain taxes also in treaty situations. For this to happen, the amendment of the double tax treaty is of utmost importance, as seen above.

Thus, bearing in mind that the right to development of states can be further fostered by the collection of income, if can be affirmed that by agreeing to amendments to double tax treaties with developing countries, to make the levying of brain drain taxes also possible in treaty situations, the developed countries would be respecting the right to development.

[40] The right to development has also been thoroughly discussed at the UN level (UN, 1999, E/CN.4/1999/WG.18/2).

[41] United Nations, General Assembly, Declaration on the Right to Development, A/RES/41/128, Article 1.

[42] The Declaration on the Right to Development was adopted by 148 countries, with 8 abstentions and one objection (United States).

Moreover, the decision to allow for further collection of income by developing countries is in line with the Millennium Development Goals and the Sustainable Development Goals, as the collected income can be used to further foster development. Finally, if treaty partners believe that the collection of taxes over emigrants would yield considerable funds, they could negotiate a proportional reduction of the aid possibly granted to the developing country. In this scenario the developed countries would be respecting the developing country's right to development, as well as their self-determination on how to collect income and to use it for their development.

The right to development can, thus, provide a conceptual framework for justifying the amendment of double tax treaties necessary to allow for the levying of brain drain taxes by developing countries.

7. CONCLUSION

Since Bhagwati proposed the establishment of a brain drain tax to curb the emigration of highly-skilled individuals to more developed countries in the 1970s, the idea of how tax measures can curb or foster brain drain/gain has been subject to considerable scrutiny in academic circles. Those that side with Bhagwati normally focus on the fairness of a brain drain tax and on the benefits that the collected income could have for the budget of the emigration state, while its detractors point that the emigration of individuals to more developed countries would also be beneficial for the individual's home state. Others focus on providing benefits for individuals to remain put or to attract residents of other states, favoring a preferential tax treatment instead of the levying of a tax as a means of combating brain drain.

Irrespective of the position taken, the focus has mainly been on the benefits and problems of the ideas for each individual state, with almost no attention being paid to its compatibility with the obligations assumed in the signing of double tax treaties. In this article we delve precisely into this issue, to assess whether tax measures focused on combating brain drain can be applied when the states involved have signed a double tax treaty based on the OECD or the UN model tax conventions. The study of this issue has shown that even though in their domestic laws states may resort to brain drain taxes to collect further income from the emigrating person after emigration, this behavior is not in line with the model tax conventions and treaties signed by the states, save in specific circumstances.

The provision of a preferential tax treatment, on the other hand, could deter brain drain without conflicting with double tax treaties, but it would not curb the loss of tax revenue from highly-skilled individuals

and it could lead to questions regarding the equity of the measure. Having the revenue collection goal in mind, if states want to levy a brain drain tax in situations involving treaty partners, it is paramount that they modify their tax treaties. In this article, we present three possible amendments to double tax treaties that could serve to maintain the tax collection rights of the emigration state over the income of the emigrating person, as well as a justification to support these amendments – the right to development.

In brief, this article shows that if states opt to levy a brain drain tax in their domestic legislation, this tax will not serve the purpose of collecting taxes over the income earned, after emigration, by emigrants who move to a state that has a double tax treaty with the emigration state, unless states also modify their tax treaties. Considering that developing countries are the greatest victims of brain drain, and thus more likely to want to introduce such a tax, the necessary amendments to the treaties can be made based on the right to development, a human right duly recognized by states and by the United Nations.

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(see especially Demsetz 1967)

(Scott and Coustalin 1995)

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T(ext): Following Ely (1980, page), we argue that

R(eference list): Ely, John Hart. 1980. *Democracy and Distrust: A Theory of Judicial Review.* Cambridge, Mass.: Harvard University Press.

Two authors

T: As demonstrated elsewhere (Daniels, Martin 1995, page),

R: Daniels, Stephen, Joanne Martin. 1995. *Civil Injuries and the Politics of Reform.* Evanston, Ill.: Northwestern University Press.

Three authors

T: As suggested by Cecil, Lind, Bermant (1987, page),

R: Cecil, Joe S., E. Allan Lind, Gordon Bermant. 1987. *Jury Service in Lengthy Civil Trials.* Washington, D.C.: Federal Judicial Center.

More than three authors

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R: Turner, Charles F., Susan M. Rogers, Heather G. Miller, William C. Miller, James N. Gribble, James R. Chromy, Peter A. Leone, Phillip C. Cooley, Thomas C. Quinn, Jonathan M. Zenilman. 2002. Untreated Gonococcal and Chlamydial Infection in a Probability Sample of Adults. *Journal of the American Medical Association* 287: 726–733.

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T: (Angell, Ames [1832] 1972, 24)

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R: Levine, Phillip B., Douglas Staiger, Thomas J. Kane, David J. Zimmerman. 2/1999. *Roe v. Wade* and American Fertility. *American Journal of Public Health* 89: 199–203.

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T: The fairness or efficiency benefits of bad-faith laws are discussed at length in *Texas Law Review* (1994)

R: Texas Law Review. 1994. *Symposium: Law of Bad Faith in Contrast and Insurance,* special issue. 72: 1203–1702.

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T: Smith (1983, page) argues that

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T: had appeared in *Newsweek* (2000).

R: Newsweek. 2000. MP3.com Gets Ripped. 18 September.

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T: (Mathews, DeBaise 2000)

R: Mathews, Anna Wilde, Colleen DeBaise. 2000. MP3.com Deal Ends Lawsuit on Copyrights. *Wall Street Journal,* 11 November.

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R: Daughety, Andrew F., and Jennifer F. Reinganum. 2002. Exploiting Future Settlements: A Signaling Model of Most-Favored-Nation Clauses in Settlement Bargaining. Unpublished manuscript. Vanderbilt University, Department of Economics, August.

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T: (Eisenberg, Wells 2002)

R: Eisenberg, Theodore, Martin T. Wells. 2002. Trial Outcomes and Demographics: Is There a Bronx Effect? Working paper. Cornell University Law School, Ithaca, NY.

Numbered working paper

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***F(ootnote)**:* CJEU, case C-20/12, Giersch and Others, ECLI:EU:C:2013:411, para. 16; Opinion of AG Mengozzi to CJEU, case C-20/12, Giersch and Others, ECLI:EU:C:2013:411, para. 16; Supreme Court of Serbia, Rev. 1354/06, 6. September 2006., Paragraf Lex; Supreme Court of Serbia, Rev. 2331/96, 3. July 1996., *Bulletin of the Supreme Court of Serbia* 4/96, 27.

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Numbering of equations, tables, and figures in appendixes should begin again with 1 (Equation A1, Table A1, Figure A1, etc., for Appendix A; Equation B1, Table B1, Figure B1, etc., for Appendix B).

No more than one table should appear on a page. Tables may run more than one page.

Tables should have brief captions. All explanatory material should be provided in notes at the bottom of the table.

Identify all quantities, units of measurement, and abbreviations for all entries.

Sources should be identified in full at the bottom of each table. Do not give cross-references to footnotes elsewhere in the article.

Figures should be provided in files separate from the text and should be clearly labeled.

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Please use the Times Roman font if there is any lettering or text in your figure. Type should be 7 points or larger.

Graphics files should be black and white.

Figure captions should be placed together on a separate double-spaced page, labeled Figure Legends.

Figures may be no greater than 10 cm x 18 cm. To avoid substantial figure reduction, keys to identifying items in the figure should be set within or beneath the figure.

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