

Tax obstacles for remote cross-border employees, implications for startups and scaleups operating cross-border.

Executive Summary

High-growth European startups and scaleups rely on equity-based compensation to attract and retain specialised talent. Fragmented tax rules across Member States make it difficult to implement a single equity scheme for employees working across borders. This creates administrative complexity, inconsistent economic outcomes, and discourages cross-border mobility, limiting the talent pool available to growing companies.

Differences in taxation at grant, vesting, and sale often force companies to redesign incentives for each jurisdiction or avoid cross-border hiring altogether, reducing operational efficiency and growth potential.

A harmonised approach, deferring taxation until liquidity, aligning vesting and holding standards, and adopting common qualifying equity instruments, would lower barriers to cross-border employment, simplify compliance, and support pan-European scaleups. Coordinated solutions, such as an EU directive, the 28th regime/ “EU Inc”, could establish a scalable, interoperable framework, strengthening Europe’s innovation ecosystem.

Background

Member States have a patchwork of tax incentives for start-ups and scale ups. Broadly, these fit into three main categories:

- Research and development (“R&D”) regimes: these are regimes which encourage companies to invest in R&D by giving enhanced deductions on research and development from a corporation tax perspective;
- Incentives for investors in start-ups and scale ups: these are incentives for investors to put money into certain investments where their capital is at huge risk. Tax advantages for investors include deductions, reliefs, or exemptions that facilitate cross-border investment and improve access to funding across multiple Member States; and
- High-growth European startups and scaleups depend heavily on equity-based compensation to attract and retain specialised talent. The EU landscape is fragmented, with each Member State applying its plan requirements to local equity schemes, making it extremely difficult to implement a single equity scheme across multiple Member States.

Incentives for employees

It is normal practice for individuals employed in start-ups and scale-ups to be offered equity in their employer. Practically, this equity is offered as “*sweat equity*” where these cash strapped companies give the employees equity in the hope that individuals accept lower wages in exchange for a future upside when the business is sold. This also aligns incentives in that the employees are incentivised to add value to the business. Although many EU countries provide mechanisms to grant equity at low initial cost, variation in taxation at grant, vesting, and sale frequently undermines the attractiveness of these plans, creating materially different economic outcomes for employees performing similar roles across Member States.

Employee Stock Ownership Plans (ESOPs) play a central role in this context. ESOPs allow employees to acquire shares, typically through options granted at a low or nominal cost, with taxation deferred until exercise or sale depending on the jurisdiction. For start-ups and scale-ups, ESOPs are particularly important as they enable companies to attract and retain talent despite limited cash resources, while fostering a strong sense of ownership and long-term commitment among employees. By linking compensation to the long-term value of the company, ESOPs help align employee incentives with those of founders and investors, which is critical in high-growth environments.

However, while ESOPs are widely used for employees, there is often a gap when it comes to senior management and C-level executives who are not founders. These individuals are key to scaling businesses and driving long-term value creation, yet the available incentive structures are often less effective in promoting long-term alignment. In many cases, companies rely on warrants or similar instruments for senior hires. Warrants typically give the holder the right to subscribe for shares at a fixed price, often linked to future investment rounds, and can be structured flexibly. However, they are frequently treated less favourably from a tax perspective and may lack the clear alignment and retention features of ESOPs, particularly where their value is more closely tied to financial engineering than to sustained company performance.

In contrast, ESOP-type structures, if extended or adapted to cover senior management, can provide stronger retention incentives through vesting conditions, clearer alignment with company growth, and more predictable tax outcomes. Developing frameworks that allow ESOP-like treatment for higher-level employees, including C-level executives who are not founders, would therefore support long-term value creation and reduce reliance on less harmonised instruments such as warrants.

Patchwork of regimes

As it stands, there is a patchwork of different local tax rules determining how individuals are taxed on equity awards, and what sort of equity awards work in a tax efficient manner in a local market. For example, in Lithuania or Czechia it is normally the case that low-cost options are tax efficient from an employee tax perspective whereas in the UK or Ireland individuals tend to be awarded by shares (which result in capital gains when ultimately sold) rather than options (which result in employment income when exercised).

This patchwork of regimes makes it hard to have a single scheme that works well across the whole of the EU which disincentives the cross-border movement of capital / employment of skilled individuals in multiple member states. This fragmentation reduces internal EU skills mobility, as employees who do not wish to move across borders often face materially worse tax treatment, plan incompatibility, or simply don't get hired, creating operational friction and a smaller effective talent pool.

Homogenisation of rules around share / option schemes

Ideally, there would be a set of rules which applied universally, regardless of corporate law status, ensuring uniform taxation on the grant, vesting, and sale of shares in companies allowing companies to easily have individuals in multiple locations who are in the same equity plan. One suggestion would be a specific set of rules which apply regardless of the jurisdiction of residence.

In case of international mobility, proceeds from share and option schemes should not suffer double taxation in different Member States or third countries. The concerned States should

ensure that they apply consistently international tax and OECD principles on the allocation of such income between different jurisdictions, for example by taxing capital gains in the country of residence.

Valuations

One issue commonly faced with share schemes is that the individuals are subject to employment income tax at the point they receive shares in their employer. This is, conceptually, fine where the shares have a low value when given to employees as there should be little dry tax at the time of award but can lead to concerns about the valuation being challenged by local revenue authorities at a later date (especially on occasions where the start-up or scale-up turns out to be valuable).

Currently, there is no mutual recognition of valuations across countries. Some VC businesses will perform individual valuations in each of their markets (costly), while some don't do that (risking their valuation to be invalid and later challenges).

A single European valuation approach for shares in start-ups and scale ups could make it easier to grant equity to employees and reduce costs/ administrative burdens.

Incentives for Investors:

Different countries have different incentives for local investors to invest into risky investments. This means that share offerings which are tax advantaged in one location will not necessarily work in another, hampering the free movement of capital and making it harder to raise money in multiple markets.

The UK has the Enterprise Investment Scheme which offers tax reliefs to individual investors who buy new shares. A company can raise up to £5m each year and a maximum of £12m in the company's lifetime (limits apply to amounts company gets from other venture capital schemes). This applies for companies established in the UK, not traded at the stock and with no investor possessing 50% of shares. Individuals investing into an Enterprise Investment Scheme company receive a 30% of investment value tax rebate, can claim a loss against income if the shares become worthless, and have no capital gains tax on the disposal of shares assuming they are held for three years.

France's Free Share regime allows managers to receive shares at no upfront cost, but the value of those shares at vesting is treated as employment income (though employee tax on such income is deferred until disposal). That vesting gain remains subject to specific employer social security charges, and managers must meet minimum vesting and holding periods before disposal. Subsequent gains on sale may then be partly re-characterised as income under France's newer rules.

Italy's management carried interest safe harbour provides a clear pathway for gains on shares to managers to be taxed as financial income at a flat 26% rate rather than employment income. To qualify, managers must invest at least 1% of the entity's capital, receive distributions only after investors have recovered capital plus the defined hurdle, and typically hold the interest for at least five years unless there is a change of control.

Germany's Profit Participation Rights (Genussrechte) operate as contractual profit-sharing instruments rather than equity, allowing managers to participate in value growth without receiving

shares. They can attract capital-income-like taxation, and deferral until exit is possible in some cases, but the structure is complex and can involve accounting and legal uncertainties. These instruments are not widely used outside Germany and can carry administrative and interpretive burdens.

Luxembourg has certain incentives including investment amortization and tax deductions for investment. However, the minimum investment levels for tax deductions of 10% are seen as barriers for smaller investors.

The Netherlands used to have tax incentives for investors had abolished them.

At the same time, differences in the tax treatment of carried interest across Member States further contribute to fragmentation, particularly where such differences depend on the legal form through which the carried interest is granted. While some regimes focus on qualifying equity instruments, the underlying principle should be that, once common requirements are met (most notably that a genuine qualifying investment has been made by the management team), the tax treatment of carried interest should not depend on whether it arises from an equity or quasi-equity participation or from a contractual arrangement.

In practice, however, divergent outcomes remain common. Where carried interest is structured through qualifying equity instruments and accompanied by an investment by the management team, it is typically treated as financial or capital income in the hands of the managers, often benefiting from preferential tax rates. In such cases, the income is generally not recognised as taxable income at the level of the AIFM or advisory company, with the consequence that the carried interest is not deductible at that level, reflecting its nature as a distribution of investment returns.

By contrast, where carried interest has a contractual nature, it is more commonly treated as employment or professional income in the hands of the beneficiaries, and therefore subject to higher taxation and, where applicable, social security contributions. In these structures, the carried interest is typically paid by the fund to the AIFM or advisory company and subsequently on-paid to the managers. Both flows are taken into account for tax purposes, with the result that the AIFM or advisory company is effectively taxed only on the net amount it ultimately retains, i.e. the portion not distributed to managers or other carried interest beneficiaries.

These differences in treatment introduce distortions that are not aligned with the economic substance of carried interest. A more coherent approach would ensure that, once qualifying investment conditions and other relevant criteria are satisfied, the tax regime applicable to carried interest is aligned irrespective of its legal form. In particular, this would imply taxation as financial or investment income (potentially at reduced rates) in the hands of the managers, combined with tax neutrality at the level of the AIFM or advisory company, except in respect of any portion of the carried interest that is not on-paid to the relevant beneficiaries. Such an approach would reduce structuring incentives, enhance neutrality, and support the objective of facilitating cross-border investment within the internal market.

Benchmark

We would suggest that the EU could create a benchmark of local incentives to avoid the complexity of building separate cases in each country. This would lead to greater harmonisation across markets.

A similar EU benchmark for employee equity plans would further support cross-border employment and harmonisation of tax treatment.

Research and development regimes / other corporation tax incentives

Many territories have R&D regimes which give an additional deduction for companies investing in R&D. This was also discussed under the BEFIT proposal to incentivise investment in specific sectors – one of the concerns around BEFIT is the lack of access to these regimes if there was corporation tax harmonisation for large entities.

The UK already has specific tax rules to encourage certain behaviours and investments in R&D. These include enhanced deductibility of R&D expenses as well as cash tax refunds for loss making companies investing in R&D.

In France businesses that spend money on R&D, including start-ups, are granted a tax credit, which can be offset against the corporation tax they owe: the rate is 30% for the part of expenditure less than €100m, above which 5% is applicable. Additionally, there are specific exemptions for young innovative companies which allow them not to pay local taxes, with some additional exemptions from employers' social security contributions, particularly for researchers, technicians and R&D project managers.

In Luxembourg a tax credit is available for qualifying investments and expenses incurred by company as part of their digital transformation or ecological and energy transition. Qualifying investments and business expenses are eligible for an 18% tax credit (while 12% is granted for new investments in qualifying assets made during the tax year), except investments in tangible depreciable assets for which the tax credit is 6%. The tax credit is calculated on the basis of the acquisition or production cost of qualifying investments made during the financial year or the amount of qualifying deductible operating expenses for the financial year.

Benchmark

We would suggest that the EU create a benchmark of how local R&D regimes should work across markets to avoid the complexity of building regimes in each member state. This would lead to greater harmonisation across markets.

DEBRA

For scale-ups, the DEBRA proposal includes a beneficial component for capital deduction on equity, despite other aspects of the proposal being more harmful for the market. This specific deduction could provide valuable support for scaling businesses.

Art. 4 of DEBRA- An allowance on equity shall be deductible, for 10 consecutive tax periods, from the taxable base of a taxpayer for corporate income tax purposes up to 30% of the taxpayer's earnings before interest, tax, depreciation and amortisation ("EBITDA").

Contact

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