



European Platform
tackling undeclared work

Sixth plenary meeting of the European Platform tackling undeclared work

Report on tackling letterbox companies

March 2019

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1. INTRODUCTION

The sixth plenary meeting of the European Platform tackling undeclared work (the Platform) was held in Brussels on 12-13 March 2019. The first day of this meeting was a thematic day dedicated to the topic of tackling letterbox companies (LBCs) in Europe, with a focus on actions by enforcement bodies, cooperation, and the role of social partners. The thematic day took forward discussions from a Platform seminar held on this topic in November 2017.¹ This report summarises the presentations and discussions at the thematic day, drawing also on the input paper prepared for participants². Two parallel workshops took place during the thematic day:

- The first was devoted to 'national approaches to tackle letterbox companies' and included presentations from Latvia, Belgium, Romania, and Hungary. The objective of this workshop was to discuss: detection of letterbox companies, deterrence initiatives including administrative sanctions and penalties, judiciary cooperation and data mining.
- The second workshop focused on 'developing effective cooperation within and across countries' and included presentations from Denmark, Finland, and the European Migrant Workers Union (EMWU). This workshop covered: cooperation among enforcement agencies, cross-border cooperation, social partner initiatives as well as education and awareness-raising campaigns.

A holistic approach to tackling LBCs was a common guiding principle throughout the meeting. This entails developing effective cooperation between all stakeholders and a combination of direct and indirect approaches and measures. This is particularly important when tackling LBCs where different 'entry points' for an investigation can be used, including a social security or tax perspective, labour law violations or a judicial route.

The remainder of this report firstly outlines the current state of play regarding LBC including the common legal background and definitions as discussed at the Plenary meeting. Section 3 then outlines some of the detection and deterrence approaches to tackling LBCs, while section 4 examines some of the preventative approaches. The final sections set out the lessons learned from these examples and possible next steps which can be taken by Member States and the Platform as a whole.

2. BACKGROUND

One of the challenges in tackling undeclared work through LBCs arises from the principle that if a Member State considers it lawful for a company to have a registered office in its territory while having its business in another country, it will also be lawful under EU company law, as long as there is not a situation of abuse. Member States apply this principle, as well as their tax and social security laws, in different ways, which consequently affects the understanding, definitions and methods to tackle LBCs.

2.1. Relevant EU principles

Most countries do not have a clear definition of what constitutes a LBC. Some clarification comes from EU rules (e.g. European Court of Justice (ECJ)) which establish 'substance' testing and provide case law on abuse of rights when addressing the problem of undeclared work (UDW) in LBCs.

¹ See also the summary / learning resource paper from this event here: <https://ec.europa.eu/social/BlobServlet?docId=18961&langId=en>

² Mireia Llobera. (2019). Tackling letterbox companies: challenges and policy options. Input paper to the thematic discussion. European Platform Undeclared Work Plenary meeting 12-13 March 2019. (Not published).

It is necessary to ascertain whether, under EU law, it is lawful for a company to have a registered office in one Member State, while having its principal base of business in another country. The first point is that EU law guarantees the freedom of establishment (of a company) within the EU. However, the definition of the *conditions* that determine a *valid* business is a free choice of law of each Member State³. This leads to several possibilities. For example, it could be required for the company to have in that country (a) only a registration; (b) only its central administration (i.e. headquarters); or (c) its principal place of business (tested through the 'substance' test). Consequently, if a Member State considers it lawful for a company to have a registered office in its territory while having its business in another country, it will also be lawful under EU company law.

How can a fraudulent LBC be identified then? The 'prohibition of abuse of rights' is a general and common-sense principle of EU Community law that ensures that EU legislation does not allow (or indeed encourage) abusive practices by economic operators⁴. An abusive practice has two elements: (1) the intention to gain an advantage from EU law by creating artificial conditions to obtain such advantage; and (2) a situation of non-fulfilment of the purpose of those laws, despite formal observance of legal requirements⁵. Fraudulent LBCs are a typical case of abuse of these rights, and abuse of workers through UDW.

The ECJ definition of employee status also establishes the legal consequences of abuse of this status. This can involve enforcing higher wages and social security and tax contributions applicable to the (real) employer⁶. This creates its own challenges as fraudulent LBCs often use chains of subcontractors or subsidiaries (in the case of groups of companies) and bogus self-employment to hide who the real employer is⁷.

Harmonizing the definition of "residence" of companies at the EU level could be a key element to tackle letterbox companies. It is also important to "clarify and align as far as possible similar notions such as 'genuine establishment', 'effective and stable establishment' 'substantial activities' and 'centre of main interest' in EU law instruments across different legal areas [...]."⁸

In this context, Box 1 below provides a working definition of LBCs.

³ ECJ judgement Daily Mail and General Trust, 81/87, pa. 19 to 21.

⁴ ECJ judgments Kofoed, C-321/05, pa. 38, and Cussens and Others, C-251/16, pa. 27.

⁵ On tax matters, ECJ judgments, Cadbury Schweppes, Case C-196/04, para. 55; 2 may de 2006, Eurofood IFSC, C-341/04, pa. 34-35. As far as Social Security is concerned, Altun, C-359/16.

⁶ ECJ Judgments Albron, C-242/09, pa. 28-32; Allonby, C-256/01, pa. 72; and Danosa, C-232/09, pa. 47

⁷ Eurofound. (2016). Exploring the fraudulent contracting of work in the European Union, p. 17.

⁸ M. Houwerzijl, E. Henneaux, E. Traversa, A hunters game: how policy can change to spot and sink letterbox-type practices, ETUC project on letterbox companies, December 2016, pp. 43-44. These recommendations have been outlined more in depth there.

Box 1. What is a letterbox company?

A LBC is understood as company which has complied only with the bare essentials (e.g. book-keeping, administration) for organisation and registration in a particular country. Its actual commercial activities are often carried out in another country. LBCs are sometimes used to enable businesses to deviate from applicable legislation, resulting in violations of labour law or collective agreements, tax and/or social security compliance, leading to undeclared or under-declared work⁹. This type of UDW usually involves non-declaration of the real employer, using fraudulent subsidiaries and/or registering bogus self-employment or bogus micro enterprises¹⁰.

LBC can also be “companies with potentially artificial incorporations where, for instance, it is questionable whether management or financial decisions are made at the place of incorporation, whilst the legal entity enjoys material benefits from the incorporation. This might include preferential treatment of income generated in other Member States or the circumvention of legal and conventional obligations in other Member States, whether legal or not”.¹¹

UDW in LBCs has often a cross-border dimension, involving (a) undeclared employment, (b) under-declared wage or working time, (c) undeclared or under-declared social security contributions, (d) non-declaration of employer status (e) and/or bogus employment contracts.

2.2. The tax dimension

A first approach to tackle LBCs is to disregard legal effects when allocating taxable profits to companies which create artificial conditions to obtain advantages (i.e. the disavowal of tax effects). In such cases, the sole activity of LBCs can be, for example, the receipt of interest and its transmission to the beneficial owner or to other conduit companies. For the ECJ, the absence of actual economic activity (a common characteristic of LBCs) must be inferred from an analysis of all the relevant factors relating to: the management of the company; its balance sheet; the structure of its costs and expenditure incurred; the staff that it employs; and its fixed assets¹².

Secondly, EU rules have established multilevel cross-border cooperation procedures, as well as general and specific anti-avoidance rules, which include substance requirements¹³. In this regard, it is important to differentiate tax *evasion* - illegal activity that results in not paying or under-paying taxes - from tax *avoidance* - technically legal activity that results in the minimisation of tax payments. In fact, since multinational companies have access to cross-border tax planning, they can lower their tax rates in ways that are not possible for domestic companies¹⁴.

Thirdly, information exchange mechanisms have also been established through Eurofisc, in addition to transparency mechanisms. Income from employment falls within the scope of such exchange of information in the EU, and databases on VAT-taxable persons and their intra-community transactions have been created.¹⁵ Finally,

⁹ European Commission. (2018). Glossary of Terms. European Platform tackling undeclared work. <https://ec.europa.eu/social/BlobServlet?docId=20304&langId=en>

¹⁰ Mineva, D. and Stefanov, R. (2018). Evasion of Taxes and Social Security Contributions. European Platform Undeclared Work, p. 11. Cremers, J. & Hastings, T. (2017). Developing an Approach for Tackling Letterbox Companies. A learning resource. European Platform Undeclared Work.

¹¹ K. McGauran, The impact of letterbox type practices on labour rights and public revenue, ETUC project on letterbox companies, June 2016, p. 12.

¹² ECJ Judgments Denmark case, C-116/16, and N Luxembourg 1 case, C-115/16.

¹³ Article 8 (a) of Council Directive 2011/16/EU is particularly relevant; also Article 6 (general avoidance rule) and Article 7 (controlled foreign company rule) of Council Directive (EU) 2016/1164; Council Regulation (EU) 2018/1541.

¹⁴ Eurodad (coord.). (2015). Fifty Shades of Tax Dodging. The EU's role in supporting an unjust global tax system. Brussels.

¹⁵ Council Regulation 2010/904/EU; Council Regulation (EU) 2018/1541.

the re-launch of the Common Corporate Tax Base (CCTB) will provide companies with a single set of corporate tax rules for doing business across the internal market¹⁶. Consolidation will also be of paramount importance to fight tax avoidance and evasion.

In general, transparency is essential to fight LBC. For this reason, ownership and financial transparency are key to tackle regulatory avoidance.

2.3. The social security dimension

From a social security perspective, some specific challenges were raised at the Plenary meeting: companies which are active in two or more Member States; the maritime sector involving sailors; and abuses in posting of workers. 'Substance criteria' to determine whether an undertaking genuinely performs substantial activities in a Member State are contained in the social security rules that apply (among others) to posting of workers¹⁷. Furthermore, case law has developed detailed criteria to tackle abuse involving LBCs and has reinforced the existing ban on the rotating replacement of posted workers¹⁸.

Issues requiring further efforts, include: (a) existing loopholes in interpretation and limited cooperation between administrations focused on UDW in LBCs; and (b) enforcement difficulties in the transport and maritime sectors¹⁹.

Finally, the lack of chain liability obligations across borders²⁰ also poses difficulties in deterring LBCs. A system of joint and several liability in subcontracting chains could be introduced.

3 DETERRENCE MEASURES

Tackling LBCs is complex. LBCs can often disappear overnight or change their names; their movements are difficult to follow and their obligations to workers are often disregarded. One of the main challenges identified in the Plenary meeting was the effectiveness of the policy tools available. Regarding deterrence measures, there were three main areas of concern:

- Detection. As outlined earlier, it proves difficult to identify a LBC and there are real issues concerning data exchange, data sharing, and data collection, using indicators specifically focused on LBCs. In this context, potential changes to the EU legal framework were also discussed.
- National and cross-border cooperation. A lack of coordination exists as regards operations and strategy designed to tackle LBCs.

3.1. How can LBCs be detected?

Several Member States presented a range of tools which they use to identify LBCs. Latvia focuses on risk analysis to detect LBCs involved in 'VAT debt schemes' (see box 2 below).

Box 2. Risk analysis to detect LBCs in Latvia

Such debt schemes concern LBCs that have declared but not paid VAT, thus accumulating a large amount of debt. Such LBCs tend to disappear quickly, start up again with no debts, and continue to trade as a new company. Three important

¹⁶ Proposal for a Council Directive on a Common Corporate Tax Base, Strasbourg, 25.10.2016, COM(2016) 685 final.

¹⁷ Article 14 (1) and (2) of Regulation (EC) No 987/2009.

¹⁸ ECJ Judgment Plum case, C-404/98; ECJ Judgment Alpenrind, Case C-527/16.

¹⁹ See also the learning resource paper from the Platform seminar on undeclared work in the road transport industry here: <https://ec.europa.eu/social/BlobServlet?docId=19913&langId=en>

²⁰ Judgment of the Court of 18 May 1995, C-327/92, Rheinhold & Mahla, ECLI:EU:C:1995:144.

preconditions were identified to detect probable tax evasion in a timely manner:

- Necessary volume of information;
- Information analysis options (IT systems and tools); and
- Human resources analysts.

Information from VAT returns provides interesting data for risk analysis on LBCs, because traders in Latvia are obliged to provide detailed information, such as: (a) names and VAT registration numbers of all clients and suppliers, (b) transaction dates, (c) invoice numbers, (d) transaction values, (e) and transaction types (import, taxable transaction, reverse charge, etc.). LBCs are identified during a subsequent risk analysis process from a knowledge-based expert system with techniques based on all available information about a taxpayer (through a computerised risk analysis system called ESKORT) combined with a transaction network analysis (using software called IBM i2 Analysts Notebook).

Indicators similar to a 'substance test' are used to detect LBCs in Denmark (see Box 3 below) and in Finland.

Box 3. Indicators used in Denmark to check LBCs

The tax inspectorate examines whether companies' day-to-day tasks and key decisions are performed in Denmark (in the context of the 'Seat of Management' project) – which are like the 'substance test' described earlier. Thorough audits are put in place, as specific aspects need to be carefully proven to establish whether the LBC abroad is fraudulent or genuine. These criteria include that:

- The 'seat' (or HQ) of the executive board is situated in Denmark;
- All-important tasks take place in Denmark: negotiations, contracts, customers, suppliers, etc;
- Key employees are based in Denmark;
- If premises are rented or the company is registered in another country, there must be few activities taking place in these other locations (i.e. the 'substance' of the company is in Denmark).
- Where the above indicators are positive it means the company is liable to pay tax under Danish law and not abroad, as it is a fictitious arrangement.

In addition, the **Finnish Labour Inspectorate applies the substance test contained in EU rules in order to evaluate whether a company genuinely performs substantial activities in the country of origin.** Furthermore, the Finnish Centre for Pensions (*Eläketurvakeskus*) enforces applicable rules on the coordination of EU social security systems²¹ when deciding an individual's social security coverage (which involves the issuance of A1 forms) during employment abroad. Such regulations provide criteria for identifying a LBC, which also includes a 'substantive activity test'.

Also in Finland, a new national online database provides an up-to-date repository of earnings, benefits and pensions data for the data authorities' decision-making processes. From 1 January 2020, the pool of data users will expand to include Statistics Finland, the Employment Funds, non-life insurance providers, unemployment funds, the Ministry of Economic Affairs and Employment's administrative branch, and the Occupational Safety and Health Authority. Such a

²¹ Article 14(2) of Regulation (EC) No 987/2009 of the European Parliament and of the Council of 16 September 2009 laying down the procedure for implementing Regulation (EC) No 883/2004 on the coordination of social security systems (OJ L 284 30.10.2009, p. 1)

register can be a tool for preventing the growth of UDW, including through fraudulent LBCs, as the register makes it possible to detect omissions in reporting payments.

REVISAL in Romania is a digital register that provides information to foreign authorities on workers who are posted abroad. The register can help identify the existence and duration of employment relationships. It indirectly helps detect UDW in LBCs as identification data on a company provides registration details to the Business Register. Cross-checking both types of data allows authorities to have useful 'hints' to detect LBCs.

While the examples presented above provide some solutions to detecting UDW, one of the main challenges still existing is examining complex datasets to identify LBCs. These common challenges are summarised below:

- The **lack of common European instruments, criteria and definitions** to identify and tackle letterbox companies;
- Improvements in **targeting** have become a priority. The use of data mining can serve this purpose through control operations that rely on data tools that utilise existing knowledge (e.g. statistics, econometrics, new tools, big data, etc.).
- While most Member States focus efforts on **data matching** (large-scale comparison of records or files collected for different purposes), fewer undertake data mining activities (finding patterns, correlations, and outliers to be used for inspections)²² to tackle LBCs. For data mining to be used as an effective tool to tackle LBCs, further investigations and developments are still required.
- LBCs are a particularly **complex hidden phenomenon, evolving rapidly**. Only estimates can be made to try to determine their **extent, cost** and **defining characteristics**. Some data is more critical and can be given a greater weighting (e.g. 'making data talk', which will be crucial to determine how LBCs 'take their decisions' and help predict future behaviour).
- LBCs can be inspected during an **on-site audit** on a case-by-case basis. This can follow-up on statistical clues provided by data analysis.

In addition, it is **difficult to acquire structured data** on UDW in LBCs, as such data are provided by different authorities with different methods.

3.2. National and cross-border cooperation among judicial authorities

Judicial cooperation can provide methods and techniques that are more effective than basic labour inspections when tackling UDW in LBCs. For example, cooperation with the police to investigate items such as bank accounts; phone numbers and telephone traffic; e-mail; IP addresses; and/or organised house searches takes inspections to the next level. In addition, with a judicial inquiry in place, any additional uncovered information can support a more robust and dynamic investigation.

Additional investigative powers can also help secure cooperation from other countries. Relevant information can be obtained on UDW in LBCs from cross-border investigations through unmanned legal aid requests; staffed legal aid requests (rogatory commissions²³); information exchange by the police (Europol), and support from the Federal Prosecutor or Eurojust. An interesting example of a unique service in Belgium in the area of judicial cooperation is in Box 5 below.

²² Thematic Review Workshop on Data Mining for More Efficient Enforcement 1 & 2 June 2017, Helsinki, Finland. European Platform Undeclared Work. p.1.

²³ Letters rogatory or letters of request are a formal request from a court to a foreign court for some type of judicial assistance, which are dealt with by rogatory commissions.

Box 5. The Belgian Labour Auditor

A unique service in Belgium exists for the investigation and prosecution of labour-related criminal offences ('the Labour Auditor', hereafter LA). The LA deals with criminal offences that may involve UDWs in LBCs such as organised social fraud (both contribution fraud and benefit fraud); non-declaration of employment or social security contributions; and/or non-declaration of employment of foreign workers. However, priority action is focused on cases involving serious and organised fictitious arrangements, involving a high number of employees and/or falsification of documents.

During the Plenary meeting, Belgium presented real case of a LBC prosecution. The investigation started with a report from the Belgian Anti-Money Laundering Committee to the Justice Department. The report indicated fraud and the use of an artificial 'mailbox address' in another Member State. The existence of social fraud and UDW involving an LBC was confirmed through thorough judicial cooperation, which involved investigating bank accounts, performing telephone taps and house searches in another country. Money was recovered through seized goods. An administrative inquiry would have resulted in the LBC being regarded as a 'debtor' of social security contributions and taxes in Belgium, would have remained unpaid.

Finally, it was noted that judicial cooperation focused on UDW in LBCs is not carried out more often due to several challenges: (a) tackling international organised schemes sometimes goes beyond the limits of the competences of the Labour Auditor; (b) getting information and doing research abroad is particularly complex and presents multiple difficulties; and (c) there are limited chances for a LBC to continue operating on a declared basis.

3.3. National multiagency cooperation

LBCs are a multifaceted phenomenon - an example presented by Denmark on their multiagency approach was shown to be particularly effective. **The Danish presentation clearly showed that using different entry points through multiple agencies offers better results for tackling UDW in LBCs** (e.g. through taxes, working environment, social security, insurances, and wages). The project, called 'Project on Social Dumping', has been in operation since 2012. It involves joint work of the Danish Tax Agency (*Skattestyrelsen*), the Working Environment Authority (*Arbejdstilsynet*), the Danish Agency for Labour Market and Recruitment (*Styrelsen for Arbejdsmarked og Rekruttering*), Police Forces and the Danish Tax Agency. In 2017 a new sub-project was developed called the 'The Seat of Management' project, which specifically targets UDW in LBCs (also described above). This project is also focused on specific high-risk sectors such as transportation and construction.

Spain also specifically tackles LBCs in the transport industry through a multiagency approach. This example is presented in Box 6 below.

Box 6. Tackling LBCs in the transport sector in Spain: 'Master Plan for Decent Work' (2018)

The transportation sector in Spain has been identified as an area of particular risk of LBCs. Spanish authorities have developed a multiagency programme that aims at tackling LBCs in this sector, based on:

- **Joint investigation and data exchange.** This is carried out by the Tax Agency, the Labour Inspectorate, the Transportation Inspectorate, the Social Security Administration and with support from other Member States. Such investigations allow fraud profiles to be developed which help labour inspections target UDW in LBCs. In addition, when fraud is detected, social security authorities contact other Member States and ask for the withdrawal of A1

forms.

- **Detection.** The Transportation Inspectorate helps the Labour Inspectorate identify inconsistencies in the number of trucks and trailers in certain companies. This can suggest that a LBC is being used, whether established in Spain or in a foreign country. The Transportation Inspectorate also has the means to inspect tachographs in the trucks, analyse routes, analyse times and perform other functions. Without such information, labour inspectors would not be able to develop effective action.
- **Whistle-blowers.** Workers can anonymously report the existence of UDW in LBCs. Companies that are victims of unfair competition also provide useful 'tips'.
- **National coordinator on posting of workers.** This position will be created to collate all information, establish a common inspection procedure, facilitate cooperation among different authorities and provide specialist support for inspectors (who are, among others, conducting checks to tackle UDW in LBCs).
- **Awareness and capacity building.** Different measures are being used: a specific campaign for inspections against UDW in LBCs, a guide (in development) which examines the inspection process, as well as specific training for some officials to become experts in this matter.

3.4. Enforcement authorities cross-border cooperation

There are promising practices of collaboration between Member States to tackle UDW. Finland's presentation showed a useful approach to cross-border cooperation. Through the umbrella of the European Agency for Safety and Health at Work (EU-OSHA), **the National Focal Point in Finland coordinates and manages their national plan to tackle (*inter alia*) UDW in close consultation with relevant EU stakeholders, including social partners.** As part of this plan, specific activities to tackle LBCs result from the implementation and adaptation of EU posting rules into the national legal system.

In addition, an agreement was concluded between the Labour Inspectorate of **Estonia** and the Finnish Division of Occupational Health and Safety of the Regional State Administrative Agency for Southern **Finland**, in 2014. **It allows inspection activities to be more effective as shared information facilitates targeted activities on UDW in LBCs.** In that sense, cross-border cooperation increases the detection of LBCs and deters abuse: cooperation agreements supported by a good network of relevant persons is found to be the basis for effective cooperation.

Effective enforcement and controls against the establishment of letterbox companies are of paramount importance, at both European and national level.

3.5. Criminal prosecution

Member States tend not to have nationally agreed definitions of what aspects of LBCs are illegal. In Hungary it's the criminal code that prohibits fraudulent activity, which is in line with the approach of the ECJ. The prosecution of these crimes perpetrated by LBCs has been particularly successful. Statistics from the Hungarian police in 2018 show that, from 211 investigations, 42 cases resulted in identification of crime, of which, 26 cases involved prosecution for disguising the economic operator 'so that it cannot be located at its registered office, permanent establishment or branch' (Section 409. 1.a of Hungarian Criminal Code). An additional 11 cases involved failure to

disclose data 'if the obligation of reporting is prescribed by law' (Section 409.2 of Hungarian Criminal Code)²⁴.

3.6. Pivotal role of social partners in tackling LBCs

Workers' and employers' associations have different roles when tackling UDW in LBCs, but both are essential. Platform members and observers at the Plenary meeting highlighted the **importance of cooperation with employers' associations in sectors where LBCs tend to be more prevalent**. For example, Latvia provides positive examples of successful work with employers' associations in the security sector.

Trade unions (employee associations) have also developed good practices. The European Migrant Workers Union (EMWU)²⁵ presentation described the implementation of a range of initiatives for tackling UDW in LBCs, including:

- Free advisory centres for workers from Eastern European countries financed mainly through public funds from the federal and regional states in Germany.
- Extensive awareness campaigns implemented in the construction, agricultural, and transportation sectors focused on preventing UDW in LBCs.
- Face-to-face information campaigns on LBCs for lorry drivers on parking lots through distribution of leaflets in different languages with information about applicable statutory minimum wages, working and rest times, daily allowances, and health insurance rules.
- Cooperation with enforcers: in particular, with SOKA-BAU (social fund of the German construction industry established by social partners) with respect to the enforcement of the mandatory holiday fund scheme in construction and with Zoll (German customs) in respect of mandatory registration of employees hired in LBCs.

Though these initiatives have been successful in tackling UDW in LBCs, the EMWU representative expressed the view that awareness efforts are **only successful if combined with effective inspections (i.e. a combined deterrence and preventative approach)**. Also, the EMWU highlighted that external funding has been crucial to their prevention work, such as the information campaigns for lorry drivers.

4. PREVENTATIVE MEASURES

Preventative measures were discussed at the Plenary meeting as having the potential to have positive effect on tackling LBCs. However, currently there are few examples - Platform members highlighted the need for additional education, awareness-raising campaigns, as well as supply-side and demand-side incentives. In addition, joint liability systems and controls over subcontractors are in many cases not sufficiently developed to deter LBCs.

4.1. Awareness campaigns

Most participants agreed that more focus was required regarding raising awareness on UDW in LBCs. The target audience for such campaigns should be chosen carefully and could include the following²⁶: employers and customers: concerning risks and costs of UDW in LBCs; suppliers of UDW: concerning benefits of formalisation; the public:

²⁴ There is also a Supreme Court decision on the issue of tackling LBC (Kúria Bfv.1871/2017/8.).

²⁵ The European Migrant Workers Union (EMWU) was established in 2004 by the IG BAU (trade union for construction, agriculture, and cleaning sector in DE) as a lobby organization for migrant workers.

²⁶ Williams, C. C. (2018). Tackling under-declared employment in the European Union. European Platform Undeclared Work Plenary meeting 18-19 October 2018, p. 9.

about problems of purchasing from LBCs; the public: for awareness on public goods and services from taxes collected; workers: including hotlines and protection of whistle-blowers, to raise awareness and knowledge of their rights; social partners: for increased understanding of LBCs' related problems and specificity of UDW in certain sectors (transport, agriculture, hospitality, construction etc.), as well as for information can be provided to trade unions and employers' associations regarding good practices on UDW in LBCs that are transferable to their sectors/countries.

4.2. Subcontracting chains

Contractors also play a pivotal role in tackling and deterring LBCs. Establishing contractors' liability and joint and several liability through the whole subcontracting chain is a necessary step forward, as it fosters contractor's control over possible unreliable subcontractors.

In Latvia, a guide exists on the State Revenue Service's website where companies can check if partners/subcontractors are bona fide. Key learning points from this include ensuring that:

- This information is in the public domain, so everyone can check how much tax these companies pay, how many staff they employ, etc; and
- There is a ratings system (e.g. on a scale from 0-100%) for other lead contractors to indicate whether the subcontractors are 'reliable' or not.

In Spain, all contractors are obliged to check their subcontractors' social security compliance history. Therefore, the contractor can be in control of its suppliers, which helps to avoid that the subcontractor amasses large debts and disappears.

5. LESSONS LEARNT

Tackling LBCs benefits bona fide employers, by ensuring a level playing field, employees, by protecting their rights, and governments, as public finances are protected. Effective examples of policy options identified at the Plenary meeting included measures to improve detection, deterrence and preventative measures to tackle UDW in LBCs. These are elaborated in Box 7 below.

Box 7. Possible policy options²⁷

Measures to improve detection

- **Administrative capacity and resources** for improved cooperation. Action against LBC requires considerable time and resources to investigate, especially when the company is established outside the territory.
- **Strengthening enforcement and cooperation between Member States to tackle abuses and letterbox companies** (e.g. in the areas of posting of workers and coordination of social security systems). In order to achieve this, **more resources could be dedicated by competent authorities and inspectorates to the cooperation requirements for cross-border matters.** The **European Labour Authority** could play an important role in this area. A **central European business registry** providing European companies with unique legal identification numbers and a European system for identifying disqualified directors as well as companies that have committed serious violations of social and tax legislation could be resourced.
- Improvement of the **quality of response** to questions on the Internal Market Information System (IMI), concerning substantial activity, assets or turnover of a company in another Member State.

²⁷ The policy option listed here were put forward during the meeting. However they do not necessarily reflect a consensus among Platform members.

- **Registers' consolidation.** Use of data-driven risk assessment based on information gathered from multiple sources (public institutions, employers, employees, clients and other third parties) on UDW in LBCs. Creation of a **European database of the infringements** committed by LBCs.
- Further development of **joint inspections** and coordinated prosecution action specifically addressed to UDW in LBCs.
- The 2015 Digital Single Market Strategy²⁸ and the 2016 e-Government Action Plan²⁹ aim at a smooth functioning of the Single Market for the duration of a company's life-cycle, when interacting with authorities concerning company and branch registration and filing of information. The business registers interconnection system (BRIS) will be part of the revised and modernised procedure. In this regard, national labour inspectorates investigating UDW in LBCs can play an active role if they can have **access to such registers**.

Deterrence measures

- Rules to hold the **actual employer** of undeclared employees liable for wages and other obligations, limiting the subcontracting and/or introduction of an 'employment guarantee' by the real employer involved in the setting up of LBCs.
- In the case of subcontracting chains involving LBCs where the contractor does not exercise powers of management, **joint and several liability** systems can also apply, notwithstanding the EU principle of proportionality.
- Directive 2014/67/EU has already launched the **cross-border enforcement of financial administrative penalties** and/or fines. Further work is needed to address UDW in LBCs through shared data sources.
- Specific changes could be introduced to the rules on social security coordination (operationalisation of the duty of sincere cooperation; more powers to the host Member State). The revised posting of workers directive should be transposed adequately (in particular with regard to the employers' duty to reimburse travel, board and lodging costs, as well as with regard to the real establishment of the company in the posting Member State).

Preventative measures

- **Harmonizing the definition of "residence" of companies at the EU level could be a key element to tackle letterbox companies.** Introduce the real seat principle and establishing certain common criteria for the definition of companies' residence.
- **Agreement on, and use of, common EU legal definitions** of letterbox companies, as well as common instruments and criteria (based on factual elements).
- **'Formalisation' advice** to start-ups and existing businesses, where officers must be trained on the detection of UDW in LBCs.
- **More transparency** could be established at European and national level. It is important to resource public registers of beneficial owners for companies, foundations and trusts. Ambitious public country-by-country reporting and a CCCTB could be introduced at European level.
- Facilitating an environment where employers **benefit by operating on a**

²⁸ COM(2015) 192 final.

²⁹ COM(2016) 179 final.

declared basis.

- **Incentives for customers** that check if the services/goods they receive come from a LBC.
- National and EU level **substance rules specific** to economic sectors and activities.
- **Tax audits** of contractors, as potential scheme organisers involving UDW and LBCs.
- Preventive measures addressed at large enterprises, as **receivers** of the services from LBCs.
- **Cooperation with sectoral associations** to learn how to control circumvention of rules by LBCs.
- **Disavowal of legal advantages** when companies fail substance tests, in application of EU posting and social security rules.
- Awareness campaigns to inform suppliers of UDW of the **risks and costs** of LBCs.

Building on initiatives in the tax area

Wide-ranging progress made under tax law can be transferred to employment policy areas. In particular:

- **Multilevel cross-border cooperation** among tax authorities to develop joint audits, sharing information and guidance can serve as a source of inspiration to enforce measures to tackle LBCs. EU tax-related platforms and networking exist for specific areas such as VAT, Eurofisc, including new channels of effective information exchange in the OECD area.
- The public and national inspection services could be allowed to know **how much business activity** multinational corporations have in each country where they operate. This is known in the tax field as 'Country By Country Reporting' (CBCR) and may help finding LBCs across borders³⁰.
- Another step could be to grant labour inspectorates access to **existing databases** put in place by tax authorities. Privacy issues and rights of citizens must be considered.
- The tax approach with regard to '**disavowal of legal advantages**' when companies fail substance tests is also transferable to tackle the social consequences of LBCs. Tax authorities can disregard the tax effects of allocating taxable profits to companies, which are fictional arrangements. Similarly, labour inspectorates could apply the law that the real employer has tried to circumvent through fictitious arrangements.

Enhanced political will

- These issues require a lot of time and resources and undeclared work in LBCs are not always a priority. Furthermore, **changes could be introduced to the current European legal framework in different areas** (in particular the incorporation requirement and the definition of genuine and substantial economic activity for the establishment of companies). Thus, political commitment is a prerequisite, at European and at national level.

³⁰ Directive 2013/36/EU; Commission proposal for a Directive of the European Parliament and of the Council amending Directive 2013/34/EU as regards disclosure of income tax information by certain undertakings and branches (COM (2016) 0198).

- In this regard, the European Labour Authority (ELA)³¹ provides an opportunity for technical and operational support.

6. WHAT MORE CAN BE DONE?

6.1. What more can be done by Member States?

- Member States could consider moving away from ad hoc joint actions towards cohesive multi-agency programmes to tackle UDW in LBCs. Multi-agency strategies offer different entry points to tackle LBCs and offer potential for excellent results.
- Member States could consider entering into bilateral and multilateral agreements for enhanced cooperation on data collation, information exchange issues and joint inspections focused specifically on UDW in LBCs.
- Enforcement authorities and social partners could pilot capacity-building and awareness campaigns for increased understanding of LBC related problems and the specificity of UDW in certain sectors.

6.2. What more can be done by the Platform?

- Provide capacity-building support to Member States in areas such as detection of LBCs, judicial cooperation or data mining, using indicators specifically focused on LBCs.
- Organise more discussions and knowledge exchanges, to enhance collaboration and sharing good practices to tackle UDW in LBCs.
- Develop activities to map different Member States' interests in LBCs, the problems that they face when tackling UDW in LBCs and possible solutions.

³¹ European Commission Proposal for a Regulation of the European Parliament and of the Council establishing a European Labour Authority. Strasbourg, 13.3.2018. COM(2018) 131 final.