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GMS Flash Alert

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United Kingdom – Impact of "Hard Brexit" on Social Security for Assignees

While the U.K.'s vote for Brexit[1] has focused much attention on the fate of the free movement of workers principle – immigration rights – social security is another important area of concern for cross-border workers and their employers.

It is important to bear in mind that European Union (EU) social security regulations will be on the negotiating table when the U.K. government and EU officials work towards an exit agreement for the United Kingdom.

WHY THIS MATTERS

It is not known whether the U.K. will continue to be able to apply EU social security regulations post-Brexit. Any change to the current regime could mean that employees are no longer eligible to remain insured in their home country regime and either host or possibly dual contributions would be payable subject to domestic rules.

Employers of globally mobile workers will need to be aware of the potential changes ahead. From a policy perspective, both international assignment and tax equalization policies will need to be updated to reflect the new rules once they are agreed. This will also impact future cost projections, which will need to be updated, and may affect salary negotiations where employees could be worse off as a result.

Background

Under current EU regulations, where an employee meets the conditions to be a "posted" (or "seconded") worker or is a "multi state" worker, it is often possible for the employee to remain in his or her home country social security system for up to five years and in the case of multi-state workers, indefinitely, as long as the fact pattern remains.

This often benefits the employee, as it means his or her social security record in the home country is unbroken, there are no gaps in future state benefits, such as state pension, family/child or unemployment benefits, and benefits continue to accrue in the country where the employee ultimately intends to return.

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The EU social security regulations were originally established as a direct consequence of one of the four freedoms of the EU – freedom of movement for workers.

Immediately following the vote to leave the EU, on June 23, 2016, there was an expectation on the part of many observers that the U.K. would remain in the wider European Economic Area (EEA) and as a result, there would be limited impact on these existing regulations. This is because the wider EEA (and Switzerland) have already signed up to and adopted much of the EU legislation.

With increasing talk of a "hard Brexit" from the EU and the triggering of Article 50 on 29 March 2017, this is starting to look less likely. Certainly, commentary from leading figures within the EU has been consistent – the U.K. will not be able to "pick and choose" free trade but not accept free movement. This means the U.K. may no longer be able to benefit from the EU social security regulations post-Brexit. This and many other areas tied to the U.K.'s membership of the EU and what the relationship will be post-Brexit will be the subject of negotiation over the next two years.

If The U.K. Is Not Part of the EU Social Security Agreement – What Then?

Whilst the possibility of a separate U.K.-EU Totalization Agreement should not be ruled out at this stage, if this was not negotiated, the U.K. still has several bilateral social security agreements in place with a number of, but not all, EU countries which pre-date the overarching EU Agreement.

However, when we start to look at the detail of these agreements, it is clear that they do not afford anywhere near the same coverage as the current EU legislation and are very limited in application. This makes sense, if one considers that the first EU regulations were enacted in 1971, when employee mobility was much more limited. It was rare for employees to commute between countries on a regular basis and business travel was not a pre-requisite for most senior roles.

By way of an example, the U.K.-France Social Security Agreement, which was ratified in 1970, states that it is possible for an employee to remain in his home country social security system for a period of up to six months. Contrast this to the five years under the current EU legislation. Where the terms of the Agreement are not met, it would appear that employers would default to the general principle of "pay where you work."

Therefore an employee seconded to France for a period of two years could end up paying social security in France rather than the U.K. as the employee would no longer meet the conditions to continue paying U.K. National Insurance Contributions (NIC). This is likely to result in significant additional costs for an employer due to high French social tax rates when compared to U.K. contribution rates.

KPMG NOTE

Agreements with other EU countries are similarly restrictive in terms of the length of time for which an employee is able to stay in his or her home country scheme. However, with employer NIC levied at 13.8 percent and up to 12 percent for employees, the U.K. has one of the lowest rates of social security in the EU. This can be compared to countries such as France and Belgium, where social contributions can be in excess of 30 percent.

KPMG LLP (U.K.) has calculated that total social security costs would increase by over £1 million per annum, where an employer has over 19 employees working in France, paying French social security rather than U.K. National Insurance (based upon remuneration of £100,000 per annum).

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Although costs for U.K. employees assigned to EU locations may increase, where EU nationals are seconded to work in the U.K., this could result in a saving for the employer if they similarly do not qualify to stay in their home country regime. Employers should therefore review their current and possible future assignments from the U.K. to the EU, and vice versa, to better understand the impact on their globally mobile population.

Will There Be Transitional Rules?

It is to be hoped that for employees already covered by the EU social security regulations there will be some form of "grandfathering" protection or transitional period while new rules are negotiated, agreed, and introduced. However, what this may look like and the periods of time any such rules will cover, are currently unknown.

We do know that for the next two years as the U.K. negotiates its exit from the EU, the existing social security regime will continue to apply, which at least provides some short-term certainty.

Looking further ahead than the next two years, many employers are now starting to plan for a three-to-five-year period and therefore may need to budget on a worst-case basis for the potential increased costs for new assignments.

KPMG NOTE

Impact on Employees

It can be argued that in many cases employees care more about their social security position than their tax position, particularly in the case of tax equalized assignees. Unlike tax, there is an expectation that an employee will get something back for his or her social security contributions, for example, in the form of future state pension or maternity/paternity benefits.

KPMG LLP (U.K.) is seeing increased questions from employees wanting to understand the impact of Brexit on their contributions and whether their contributions made in one EU country will continue to be taken into account if they are living/working in another EU country.

It is also worth noting that although this article has focused primarily on contributions, there could also be an impact on an employee's benefits entitlement. This covers not only the state pension and unemployment, but also wider issues, including potential medical coverage currently available via the EU Healthcard.

Employer Considerations

Employers should be very cautious at this stage of over-promising in respect of what is simply unknown at the current time. Currently, we recommend that employers begin reviewing standard terminology in assignment policies and secondment letters to determine that they are not leaving themselves open to a potential claim in future. (In our experience, many assignment policies state that the employer will keep the employee in his or her home country social security system for intra EU/EEA moves.)

In light of the above-noted potential impact on employee's benefits regarding medical coverage, where there is a loss of coverage, employers may also need to compensate or provide alternative private coverage, which may increase costs.

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Back to Future? Social Security Agreements Redux

In the longer term, if the U.K. does have a "hard Brexit," it would seem likely that the U.K. will seek to update existing social security agreements across the EU if these are not renegotiated on a wholescale basis as part of the EU exit negotiations.

However, similar to double tax treaties, social security treaties take time to negotiate and ratify, which could leave a period of time where all that is left to rely on is the "old" pre-EU legislation unless a grandfathering or transitional period is agreed.

Unfortunately, it may be optimistic to expect social security rights for highly-paid expatriates (as they may be perceived) to be too high up the "to do" list of the EU or U.K. government in the short term. That may mean all that remains to work with is unwieldy and out-of-date legislation for longer than one would wish.

FOOTNOTE:

1 For prior coverage, see GMS *Flash Alert* 2016-073 (27 June 2016).

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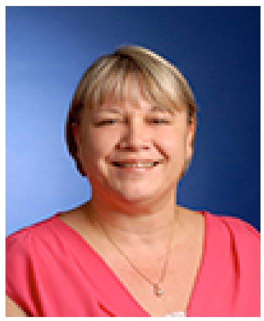

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