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'Top Ten' global mobility issues for Tax Directors to think about

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What's changed?

Mobile workforces fill a critical business need—requiring organizations to get talented employees on-site where needed, often at a moment's notice. However, cross-border employee mobility is experiencing **incredible change** and, as a result, its implementation is becoming increasingly complex.

Consider the following example...

Company X is a large, global organization that has a small traditional mobility program. However, a payroll audit highlighted large numbers of short-term business visitors traveling to the United Kingdom and this resulted in a significant tax and penalty assessment. The corporate controller was concerned about this risk area and requested a study that found Company X had an unexpected number of personnel traveling to 35 countries each year. HR and Tax executives were surprised to learn that Company X had 50 times more cross-border, international business travelers than it did on traditional relocation assignments.

The discovery led to a review of many of the key issues highlighted in the 'Top 10' including corporate level withholding and income tax obligations, and personal tax and reporting obligations of impacted travelers.

How mobility happens is quickly evolving...

Not only are businesses demanding much greater employee movement across borders, but how this migration is taking place is transforming. The number of traditional relocations to satisfy business needs is shrinking, while the use of *frequent business travel* is exponentially increasing in an unexpected way, surprising many organizations.

Other non-traditional mobility methods are also expanding, including project workers, commuters, and individuals employed by central business models (e.g., global employment companies). In addition, new alternative work arrangements in this 'Gig Economy' are arising, such as temporary workers, remote workers, and contractors.

How are companies responding?

Companies often struggle to keep up with the business' demand for mobility while ensuring proper compliance and a keen eye on cost. Each mode of mobility, such as frequent business travel, can create its own variety of both individual and corporate level tax issues that can be difficult for the enterprise to track. Tax considerations are intertwined with other matters such as immigration requirements, corporate mobility policies, and a lack of proper processes—all creating unexpected challenges for the organization.

Change can bring opportunity

This fast-paced environment can present opportunities for forward-thinking organizations. Although historically Tax Directors have been less engaged with mobile workforce tax matters, this is changing—leading Tax executives are recognizing the heightened compliance concerns associated with, for example, expanded non-traditional mobility patterns. They are responding with automated solutions and a more hands-on and coordinated approach by a cross-functional team in order to achieve efficient processes, cost savings, and more informed decision-making.

Global frameworks are changing swiftly...

At the same time, the global regulatory environment is fundamentally evolving. Legislative and regulatory changes and their enforcement—such as those enacted under the BEPS initiative, recently enacted US tax reform, and shifting immigration policies around the world—are generating tax and other compliance challenges and risks that must be properly managed. The focus of governments and tax authorities on ensuring companies and individuals pay their fair share of tax has never been higher.

The bottom line...

Top management typically taps the corporate tax department to manage global tax compliance risk and this should include understanding areas related to mobility that can require in-depth analysis and may potentially increase enterprise-wide risk.

1. Cross-border employment structures and related documentation

Starting point for analyzing tax liability and risk

Global organizations use a variety of employment structures to move talent across borders. Corporate tax departments should be involved when deciding the proper employment structure for globally mobile employees and how such structures should be implemented (e.g., proper documentation.) Employment structures are a critical step to support desired tax and risk management positions, impacting both corporate and individual-level taxes.

Examples

Many companies adopt a so-called home country model that attempts to maintain a 'legal' employment relationship with the home country employer and loan or 'second' the employee to the foreign affiliate. This may allow the employee to continue their employment relationship with the home country employer for continuity and consistency of benefits while providing a link to the host country employer for execution of assignment related activities (wage withholding and reporting, assignment related benefits, etc.) Other companies may opt for a home/host agreement with salary being delivered by more than one entity making the determination of the ultimate employer a critical factor.

The structure should have substance and reflect the reality of the employee's activities and which entity is benefiting from the services. Special consideration should be given to the cross-charging of costs and substantiation of corporate tax deductions. The employment relationships should be clearly documented to help substantiate the employer relationship, the entity benefiting from the services, and the process by which intercompany charges should be facilitated.

Proper documentation

Typically, an assignment letter is issued to the employee that documents the duration of the short-term move and explains the international benefits being offered. Assignment letters do not always expand upon the individual's relationship with the host country entity or even state who the employer is. Proper intercompany documentation of the facts can help to address potential misunderstandings with respect to whether the employee's activities create corporate tax exposure. Upfront analysis allows the corporate tax department to weigh in on more complex assignment scenarios.

Contemporaneous documentation also enables the entity to be better prepared in case of an audit. This documentation often serves as a preliminary roadmap for auditors that are seeking substantiation for deductions and proof of compliance with transfer pricing requirements.

Actions to consider

Companies need to choose and document efficient cross-border employment structures that enable tax, business, and other compliance needs. The process starts with asking a variety of questions that should drive the necessary documentation. Which entity should be treated as the employer of the assignees and for what purpose? What is the expected compensation and benefits cost allocation between related entities during the assignment period? What entity will ultimately bear the labor costs and claim the tax deduction?

The documentation of employment relationships should make clear what the inter-company service relationship is between the home and host country entities as well as the relevant employment relationships. It should also clarify which entity, if any, has the requirement to operate withholding for personal tax and social security obligations on employment income. Whatever intercompany agreement is put in place, it is not a substitute for the international assignment letter issued directly to the employee. The two should be in harmony and not contain any conflicting statements.

2. Permanent establishments (PEs)

Increased scope of PE-causing activities: Additional costs and challenges can result

Globally mobile employees can create a significant PE risk for the enterprise. The unfortunate result can be the requirement to register the company as a taxpayer, file local country returns, and remit taxes, most notably corporate income tax. Companies may mistakenly think their mobile workers in a specific jurisdiction do not have any individual tax liabilities. Unfortunately if the employee activity creates a PE for corporate tax purposes, this could mandate that individual tax liabilities be remitted.

The imposition of foreign corporate income tax, by itself, may or may not be an important financial concern for the company, depending upon its structure, foreign tax credit position, and the specific tax rate and international tax rules applicable. However, Tax Directors should remain vigilant for other potential consequences. The failure to remit such taxes properly could result in interest, penalties, and other unexpected costs and sanctions. Some tax authorities will increase their scrutiny of taxpayers that do not show compliance, e.g., by increasing their risk rating. There may also be reputational risk if such information is made public and a company is viewed as not 'paying their fair share' of tax.

BEPS initiative places additional spotlight on PE issues

The Organization for Economic Cooperation and Development (OECD), along with the G20, has developed a framework of actions to address the threat to tax fairness and tax revenues caused by base erosion and profit shifting (the so-called BEPS initiative). The intended aim is to ensure that profits are taxed where actual business activity is performed and value is created. Actions by governments under the BEPS initiative are creating fundamental changes to the international tax environment with direct implications to mobile workforces. Tax authorities are likely to be more focused on whether companies are creating PEs.

Under the BEPS initiative, changes were proposed to the definition of a Dependent Agent (DA) PE. These broadened the definition to include individuals, sales agents, and contractors who may be habitually performing activities in a location that, in the aggregate, play a pivotal role in the negotiation and conclusion of contracts executed in other tax jurisdictions. As a result, the number of cases where individuals can create a DA PE are likely to increase, creating additional risk for employers of mobile workers.

There likely will be an increased focus on intercompany service agreements for internationally mobile employees and on ensuring recharge arrangements reflect the arm's length value of the services performed. Specifically, certain skilled employees with specific knowledge who move between countries (by transferring between entities or under a secondment arrangement) may be considered to be moving intellectual property. Tax Directors should consider whether intercompany pricing of services between entities reflects such value, as well as maintaining the proper underlying transfer pricing documentation and agreements.

Actions to consider

The BEPS initiative requires a greater level of diligence around documentation and the employment structure supporting cross-border employment activity. Companies need to have controls in place for tracking and reporting mobile employees and understanding the nature of the activities being performed. Maintaining appropriate transfer pricing policies, ensuring that recharges are in line with the transfer pricing guidelines, and accurately reflecting the reality of the work performed/value created in each jurisdiction will require input from corporate tax.

Corporate tax should also involve HR and global mobility teams early in any discussions concerning foreign operations and international tax planning where individual activities are required on the ground to ensure that business substance is established and maintained. It is important for tax and HR to be in communication and form a holistic approach since there can be tensions between the optimum position for corporate and personal tax purposes. For example, arguing that the individual is acting on behalf of the 'home' employer to retain the possibility of claiming treaty relief may be completely at odds with the argument that no PE has been created.

Disclosure and transparency of work locations

Organizations will need to report a number of specific pieces of information under so-called country-by-country reporting, including the number of employees in a particular location. Given the increased sharing of information between tax authorities, this information will provide roadmaps for tax audit purposes. Having the ability to track where employees are working, as well as understanding what their activities are in-country will be even more critical going forward.

Mitigation of PE risk

As a general rule, properly executed international employee secondment agreements (and/or local employment agreements) that align the economic cost of the mobile employee's compensation and benefits with the income statement of the foreign affiliate benefiting from the services provided can go a long way to minimizing PE risk. However, for more senior employees, or individual relocations to new jurisdictions, the corporate tax department should take care to review the terms and conditions of the foreign relocation and weigh in on the proper allocation of income generated and expense attributable to the assignment.

3. *Withholding and payroll compliance*

Heightened scrutiny by tax authorities prompts need for robust processes

Payroll compliance is a key area for audits in many countries, particularly where the country derives a significant share of revenue from payroll withholding and social security taxes. Increasingly, tax authorities are looking for ways to reduce their cost of tax collection and increase tax compliance by placing the onus of enforcement on the employer. Compliance, however, can be especially challenging as it relates to mobile employees since it often entails complying with payroll obligations in more than one jurisdiction (home and host countries).

Benefits of strong process controls

The capability to accurately report global compensation is becoming a priority for businesses that want to lower their tax compliance risk—the integration of automation is typically a key component. Doing so can present the potential for significant cost savings, over and above the costs associated with not remitting the proper tax amounts. Organizations that can demonstrate robust reporting and withholding processes may be able to obtain approval from tax authorities in certain jurisdictions to exempt specific populations from the requirement to file an individual income tax return (e.g., business travelers) through a so-called cooperative compliance agreement.

Conversely, the inability to accurately report global compensation can create significant tax exposure for the organization. The potential result of noncompliance may include unexpected tax and other costs: interest, penalties, and a drain on resources if an audit occurs.

Tracking residency for withholding purposes

The question of when withholding obligations stop and start is a critical one for mobile individuals. For example, in the United States, this can be a complex analysis with respect to state and local withholding requirements. Many states have rules that define state residency during temporary assignments, allowing an employee to 'break residency' with that state if certain requirements are satisfied. Many employers, unaware of the employee's personal situation, often stop US state and local withholding when the employee commences work outside the United States. However, US state and local income tax may still be due because the individual fails to meet the requirements to break residency, i.e., an unanticipated residency status due to a spouse who remains in the home country or in-state work days during the assignment period.

For companies with employees going into the United States, complying with US payroll withholding and reporting requirements can be a challenge, especially for an organization with limited US operations. A recent trend is the use of Professional Employer Organizations (PEOs), a third party company that technically 'employs' the workers of several companies. PEOs oversee all HR-related functions, including payroll administration and tax reporting responsibilities for their clients.

Actions to consider

Employers should evaluate whether they are properly fulfilling their global payroll obligations, which can include withholding, social tax obligations, as well as reporting requirements. And they should seek an understanding of the common pitfalls in the jurisdictions in which they have more significant operations. Even the most well-meaning employer can get caught by non-familiar issues such as non-calendar tax years or positions that seem counter-intuitive. For example, in some territories, a withholding obligation can exist for the employer even though the employee is eligible for treaty relief. Lack of compliance with these obligations can result in penalties and interest for the company—costs the corporate tax department wants to avoid.

Specifically regarding the United States, companies should review the US federal, state and local, and FICA tax withholding obligations for their US-based international assignees. Their careful review of these US tax rules should also enable them to properly advise employees of their exposure to state and local taxation. If the employee claims to be a state nonresident or a nonresident alien, certain documentation may need to be filed.

Businesses should be aware of a special withholding tax rule intended to help ensure the US government's ability to obtain tax revenue. For example, there is a new 10% US federal withholding tax that generally applies if a nonresident alien taxpayer sells or exchanges an interest in a partnership that was engaged in a trade or business in the United States. The new law treats the sale of the partnership interest as effectively connected income (ECI) and, therefore, subject to US federal withholding tax. (Note that as of the time of writing, the IRS had delayed implementation of these withholding rules as they relate to publicly-traded partnership (PTP) interests).

4. Deductions for stock-based compensation

The importance of intercompany equity charge-back agreements

Stock-based compensation (such as option rights and RSUs) granted by a parent corporation may not be deductible at the foreign affiliate level for corporate income tax purposes unless active steps are taken to recharge the cost of the stock award to the foreign affiliate in exchange for a cash payment from the affiliate to the parent. This is the case generally—even where the foreign-based employee has been subject to personal income taxation on the full fair market value of the stock award, usually at vesting/transfer.

Claiming the income tax benefit

US GAAP and international accounting standards generally require the stock-based awards to be recognized (amortized) as an expense on the books of the corporation over the vesting period. The ability to claim a cash corporate income tax benefit for the compensation amount to be realized by the employee at vesting/transfer can be an important consideration in minimizing costs to the organization.

Mobile employees can create additional complexity as they may have moved between jurisdictions during the award vesting period. Generally, the entity (or entities) benefiting from the services of the mobile employee should bear the cost of the stock-based compensation.

Withholding on awards

Depending on the method used to account for such awards in the United States, it may be necessary to determine whether the method of settling stock awards creates unintended liability accounting owing to limitations on the rate of tax withholding that may be applied. In general, US GAAP (ASU 2016-09) allows employers to 'net settle' stock awards and use its own cash to fund withholding taxes up to the employee's maximum statutory individual income and social security tax rate(s) in the relevant jurisdiction(s)—regardless of the tax withholding rate otherwise applied. Open market sales of shares at settlement also provide flexibility on the tax withholding rate that may be applied to international employee stock awards.

Actions to consider

As a general rule, equity recharge agreements should be established to ensure that the foreign affiliate benefiting from the services of the employee bears the fair market value of the stock-based compensation delivered to the employee. The agreement should be clear on the allocation method of the cost connected to the stock-based award where the employee provides services to more than one affiliate during the stock vesting period. US-based organizations that previously did not recharge equity due to a full foreign tax credit position should review this approach in light of US tax reform and the transition to a territorial system.

As noted above, stock awards may be 'net settled' where shares are provided to the employee net of withholding tax. The company should review whether the withholding rate used is limited to the maximum individual tax rate in the relevant jurisdiction, particularly in the case of individuals who have moved between countries during the vesting period or who are covered under a tax equalization policy. Rate changes should be monitored. For example in the United States, withholding tax rates including supplemental tax withholding rates have changed due to the enactment of tax reform.

The company should also establish a system to track its mobile employees, allocate equity compensation, and ensure payrolls in the applicable foreign locations are equipped to meet the relevant tax withholding and information reporting requirements. The requirement to withhold is a key area of focus for many tax authorities for the simple reason that they realize many employers struggle to get it right with respect to internationally mobile employees. Companies should recognize the various traps for the unwary, such as social security obligations that are not levied uniformly across jurisdictions.

From a broader perspective, the charge-out of any employee compensation costs should be closely monitored, especially for 'C-suite' executives. Opportunities may arise depending upon the country's specific laws—for example, recently enacted US tax law restricts the US corporate income tax deduction for compensation paid to the CEO, CFO and top three highest paid executives of public companies to US $1 million. The elimination of the so-called performance based compensation exception may result in increased US corporate income taxes payable (as well as the write down in value of related deferred tax assets for financial statement purposes)—unless a portion of these compensation costs can be recharged to foreign subsidiaries that benefit from some portion of the services.

5. Deferred compensation and foreign pension arrangements

Detailed analysis and complexity can arise

Deferred compensation arrangements under one country's law are not necessarily tax deferred under the laws of another jurisdiction. Companies may not be aware of the technical difficulties in achieving a deferral under foreign law and, thus, compensation may become taxable at vesting to employees. This may occur despite the fact that no cash payment has been made to the employee to fund the tax. The result: unforeseen tax costs that could be passed on to the employer under the terms of a tax reimbursement agreement.

Actions to consider

Deferred compensation plans should be reviewed for effectiveness in non-US jurisdictions and non-US plans should be reviewed for US compliance where participants may be (or may become) US taxpayers. These plans have created the need for companies to manage compliance in multiple locations for a single employee who has relocated and earned compensation in several countries. Companies may consider modifying such arrangements or discontinuing their use for certain employees.

The application of Sections 409A and 457A should also be reviewed to determine if modifications can be achieved to avoid accelerated US taxation and/or penalties. Note that any company with a contractual vesting clause in their deferred compensation plan (e.g., age plus years of service results in immediate vesting) may need to focus on Section 457A for US employees working for the benefit of a foreign affiliate in a non-treaty country.

Foreign pension plan participants who are US taxpayers should be identified to determine whether they may have US taxable income resulting from plan participation. Form W-2 reporting requirements should also be reviewed. Where individuals are in plans potentially covered by a treaty, the terms of the treaty should be reviewed to determine whether and to what extent relief is available. For example, relief may be limited to the host jurisdiction only, which can create unexpected tax costs.

Example – where mobile employee is a taxpayer in the United States

From a US tax perspective, Internal Revenue Code Section 457A creates special issues for companies where vesting of deferred compensation rights occurs but payment is deferred in certain countries that do not have a tax treaty with the US and/or where the organization itself is subject to limited taxation. Overseas deferred compensation arrangements, similarly, should be reviewed for compliance with Section 409A where employees are sent to work in the US or where US citizens are locally employed by a foreign entity.

In addition, global organizations often employ foreign nationals in the United States who remain covered by a corporate retirement program in their home country. These foreign pension plans may have preferential tax treatment under local tax laws; however, they generally don't meet the 'qualification rules' for preferential treatment in the United States. In some cases, where the foreign plan is both funded and vested, there is a potential US tax liability (and employer reporting requirement) under Section 402(b).

If the individual is a 'highly compensated' employee, it may be necessary to capture taxable income from the 'accrued vested benefit' (which includes the growth in value), even where there are no current employer contributions. A number of treaties provide for favorable tax treatment of employee contributions, employer contributions, and growth in foreign plans, as well as providing for corporate tax deductions where otherwise not available. Rules can differ widely so individual treaty analysis is required.

Another consideration is whether Section 409A applies to the foreign plan as foreign plans that do not qualify for the treaty or the broad-based retirement plan exceptions are left with very few options. The consequences of failure to comply with these rules can be significant.

Various types of compensation and benefits are offered to employees—e.g., variable payments are typically made either in the form of non-guaranteed bonus awards or stock-based payments. Leading companies develop a baseline cost estimate of their tax equalization expense and formalize an ***accounting policy*** *to deal with the variable pay components. Budgeting can help with accruing costs, however the tax costs also need to be accrued on the books of the 'correct entity' and reconciled as actual tax payments are made (updated annually).*

6. *Information reporting requirements*

A growing trend by countries seeking greater transparency and revenue

More countries are enacting or promulgating foreign financial asset information reporting requirements for individual taxpayers—this may cover not only foreign bank accounts, but also assets held outside of that country. Governments are seeking to boost their revenue through these disclosures to ensure that they are receiving their proper share of tax associated with these assets. Examples include the United States, India, Japan, and Spain.

Compliance with these requirements can be daunting for foreign nationals on assignment and generally increase the complexity and cost of compliance for companies covering tax preparation expenses for their mobile employees. Additionally, penalties levied for the failure to report such assets can create unexpected costs to the business.

Example – FATCA reporting requirements in the United States

The Foreign Account Tax Compliance Act (FATCA) was enacted in 2010 in the United States to address noncompliance by US taxpayers using foreign accounts. One mechanism implemented to combat noncompliance is requiring foreign financial institutions (FFIs) to report information to the IRS about financial accounts held by US taxpayers (or by foreign entities in which US taxpayers hold a substantial ownership interest). FFIs can register directly with the IRS or comply with FATCA intergovernmental agreements.

Section 6038D, enacted under FATCA, creates complex information reporting requirements for certain US citizens or resident individuals that hold Specified Foreign Financial Assets (SFFAs). This provision mandates the reporting on IRS Form 8938 of a broad array of foreign assets, not just foreign bank accounts, and expensive penalties for noncompliance may be levied. For example, if a US citizen or resident holds an interest in a foreign pension plan, that interest may be reportable. In addition, certain deferred compensation arrangements offered by non-US parent companies may be reportable under these rules.

US FBAR forms also may be required

Mobile employees also may have a requirement to report foreign financial accounts on FinCEN Form 114, (so-called FBAR) in the United States. This filing is required if a US person has certain financial interests or signatory or other authority over certain foreign accounts. From a practical perspective, much of the same information may need to be reported on both forms (Form 8938 and FinCEN Form 114); nonetheless, there are key differences requiring attention to detail.

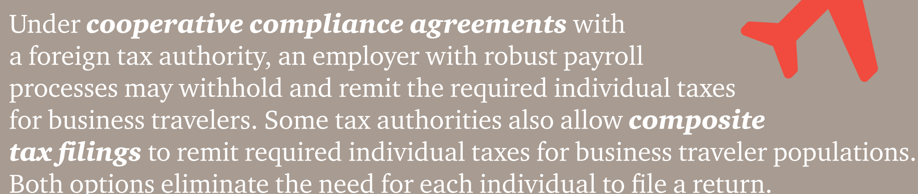
Actions to consider

Companies should understand the information reporting requirements for both home and host jurisdictions for their mobile workforces. The expected deluge of information to be received by revenue authorities from initiatives such as FATCA and CRS (the Common Standard on Reporting and Due Diligence for Financial Account Information proposed by the OECD) is prompting governments to sharpen their focus on international issues and increase penalties for noncompliance.

Specifically with respect to the United States, companies should understand the process for completing IRS Form 8938 as required by Section 6038D and raise questions regarding compliance in this area. They should also stay abreast of the reporting rules connected with employees who have signature authority but no financial interest in certain employer-owned foreign accounts.

7. Frequent business travel

This critical business need can generate tax compliance risks



Under ***cooperative compliance agreements*** with a foreign tax authority, an employer with robust payroll processes may withhold and remit the required individual taxes for business travelers. Some tax authorities also allow ***composite tax filings*** to remit required individual taxes for business traveler populations. Both options eliminate the need for each individual to file a return.

Frequent business travel allows companies to have a highly mobile workforce while being cost effective, making it an attractive alternative to the traditional assignment. While this sounds appealing, companies should be aware that tax authorities are continuously looking to increase their tax base by targeting these nonresidents conducting business in their jurisdiction.

Difficulty tracking tax compliance obligations

Business travelers are generally not part of the traditional mobility program and are often not on the 'radar screen' of HR or corporate tax. Business units may incorrectly assume that if an individual spends less than a specified number of days in a particular tax jurisdiction (usually 183 for international purposes), there are no tax consequences resulting from the individual's activities. This is often not the case since the business traveler may not be resident in a treaty partner country that contains favorable thresholds for incurring tax. In addition, depending on the structure of the assignment or the enterprise itself (for example, certain branch structures), an individual may not be eligible to use the treaty.

What adverse consequences may arise? In addition to incurring individual income and employment taxes, the nature of the individual's activities may create corporate income and value-added tax exposure in the host country or state. This may occur even if the time spent there is relatively limited. These concerns apply equally to inbound and outbound mobile executives.

Business travelers required to file a tax return in a foreign jurisdiction generally will need a taxpayer identification number (in the United States, this is an individual taxpayer identification number or ITIN, as the traveler may be ineligible to have a social security number). Each country will have its own processes but in many countries, these numbers are becoming increasingly difficult to obtain.

Heightened scrutiny by tax authorities

Tax Directors are becoming increasingly concerned about the potentially adverse tax consequences caused by these travelers. Countries and localities are expanding their audit activities due to their need for revenue to fund fiscal deficits. Audits related to PE and employer withholding and reporting are becoming more frequent and intense. Tax authorities may inquire about company personnel and their in-country presence. The company's task of compiling such information in response may be very challenging if no process is in place to track this information.

Cross-state business travel within the United States

Business travel between states within the United States, can also present risks and additional complexity for corporate tax teams. Certain states (e.g., New York) are particularly focused on mobile populations. Wage withholding and reporting compliance for this situation is a routine part of New York and other state payroll tax audits.

Actions to consider

One of the most significant challenges is that the company may not be aware that they have frequent business travelers creating cross-border compliance liabilities, and are surprised to know how many they actually have. Companies should consider establishing a monitoring program in order to document and understand travel patterns and areas of potential exposure.

Once cross-border business travelers are identified, companies should review the activities of such employees to determine whether there is any tax exposure at either the individual or corporate level. For international travelers, a treaty may provide relief from personal income tax for short term business travel under the dependent personal services article. However, to claim such relief, most treaties tie personal income tax liability to whether the corporate employing entity has a PE in the host jurisdiction, a conclusion only the corporate tax teams are likely to know.

Problems can also arise because the assumption that treaty relief is available in the host location is increasingly coming under challenge. The adoption of an 'economic employer' definition for purposes of treaty relief is becoming the norm with many tax authorities. If this occurs, liabilities can arise in host locations from day one and although credit for host location tax may be available, the administrative burden required for compliance can be complex and costly.

In addition, companies must consider whether employment costs are recharged to an affiliate (directly/indirectly) in the country where the individual is working. The treaty may also look at the length of time that services are provided to determine if corporate tax is due. For example, is the traveler part of a larger group of employees working there and perhaps part of a plan for a long-term presence in that country?

Consistency is also important—what is presented for tax purposes should be consistent with other representations being made to relevant authorities such as for immigration purposes and in Europe, for compliance with the 'Posted Workers Directive.' This requires companies to plan ahead and not simply address problems after they have arisen.

8. Entering new markets

Upfront planning for mobile workforces is critical for corporate growth agendas

Growth objectives are a critical goal for many multinational enterprises. However, cost containment is also a top priority. When businesses embark on new business opportunities, such as entering new markets, Tax Directors should advise not only on the appropriate corporate structure, but also take into account how mobile workforces will be part of the operation. For example, will mobile employees cross borders to get the operation up and running? Have the appropriate work authorization visas been obtained to allow the company to be compliant from a payroll withholding and reporting perspective? What mobile workforces will be part of the final business structure?

Unexpected assignment costs

Mobile workforce-related costs frequently come as a surprise to business units and management. This is especially true for mobile employees covered under tax reimbursement or equalization policies. Cost estimates for mobile employees can be generated to help the business make informed decisions as to cost. Special consideration should be given to those senior executives needed to implement the project as their related tax and assignment costs are likely to be significant. Advanced planning can help minimize these costs, such as when certain compensation is awarded.

Leading companies develop a baseline cost estimate of their tax equalization expense company-wide and formalize an accounting policy to deal with the variable pay components. They typically develop a methodology for maintaining and reconciling accurate budgets and accruals.

However, Tax Directors may wish to confer with their company's mobility professionals about how to avoid any unexpected increases to cost estimates generated for the project under the current mobility policies. For example, large tax equalization and gross-up payments may occur that are not properly budgeted. To avoid them, companies may consider:

- limitations on reimbursement of employee tax amounts in the case of non-company income
- special rules for employees who are separated from employment but who remain resident in a foreign location, i.e., so they are not able to expose the business to increased tax gross-up costs on final tax equalization settlements
- policy language regarding any delayed tax reimbursements pursuant to Section 409A.

Employment structures and associated enterprise-level tax risks

The most efficient employment structures for mobile workforces in any new market should be determined upfront, along with a strategy of what foreign taxes should be remitted and by which entity. This should include not only corporate income tax, but a variety of other enterprise level tax obligations that may be generated by mobile workforces. Most notably, value-added type taxes can apply if the entity that employs the mobile workers performs services for the related entity that holds an outside contract to customers. Failure to identify and report these obligations can result in interest, penalties, and other unexpected costs for the business.

Actions to consider

Companies should ensure that mobile workforce costs, efficient employment structures, and related planning opportunities are determined upfront and considered in new market decision-making. Mobility professionals should be included in the core planning team at all stages so that if management alters the growth agenda or implementation plan, any mobility-related cost impacts can be identified.

Companies should prepare cost projections at the pre-assignment stage to provide the business unit and management with an estimated budget relating to mobile employees and allow the business to make decisions around the compensation elements and benefits to include in the assignment package. Cost estimates should be refreshed for changes to equity compensation and personal circumstances, as well as new external variables such as exchange rate fluctuations and changes in tax legislation. Trailing liabilities related to deferred compensation, such as equity, can also necessitate the preparation of revised cost estimates even after an assignment has ended.

9. *Acquisitions and dispositions of business interests*

Risk assessments should take into account potential liabilities associated with mobile employees

Due diligence of pre-closing liabilities is a critical part of any acquisition or disposition transaction between unrelated parties, irrespective of whether stock or assets are transferred. Although 'known liabilities' are generally disclosed, there are various mobility-related liabilities that can be unforeseen and create unexpected costs for the parties that should be taken into account before closing. Companies unaware of these potentially large liabilities may be in for a surprise if these liabilities either come due or are discovered upon audit by tax authorities after closing.

Examples of potential risk areas

- Payroll reporting compliance for mobile employees—including social security and income tax
- Corporate income tax filings obligations connected to mobile workforces
- Individual income tax reporting failures by the employees
- Acceleration of stock vesting in a home and/or host country upon a change of control (acceleration provisions may be included in the equity plan, severance or retention agreement, assignment letter or employment agreements; some countries, irrespective of these provisions, may trigger accelerated vesting based on local laws and increase the tax equalization cost associated with mobile employees)
- 'Parachute payments' paid to mobile employees and any Section 280G/4999 rules in the United States or similar so-called golden parachute payment tax issues connected with a change-of-control.

Actions to consider

Companies should consider including in their pre-transaction risk assessments potential trailing liabilities and a target company's adherence to reporting requirements related to mobile employees. Global mobility teams are seldom brought in during the due diligence phase when negotiating an M&A transaction. The corporate tax team is typically at the table and should consider pulling in the relevant expertise as early as possible to help identify potential areas of exposure.

Organizations should understand the process for complying with rules under Sections 280G and 4999 in the United States as well as any accelerated vesting implications in the foreign jurisdictions where the target company is operating.

10. Payment of international director fees

Withholding and other tax obligations should be keenly tracked

Multinational corporations seeking a global perspective often have directors on their boards who are resident in other countries. Nonresident directors can present a number of unique tax withholding and reporting issues that will depend upon the jurisdiction involved. For example, the income tax and payroll withholding obligations vary by country and by treaty so an analysis of the domestic rules of the countries in which the nonresident board member is performing services and the applicable treaty is required.

Example of withholding obligations – United States

For a nonresident on the board of a US company, a key issue is the determination of the US source portion of any director's compensation where the individual is a nonresident and duties are performed both in the United States and overseas. Similarly, many US citizens are now on the boards of foreign companies and the terms of certain treaties can result in fees for meetings held in the United States being treated as sourced to the country where the company is resident.

Unless exempt from US tax under a tax treaty, a nonresident director of a US company will generally be subject to US federal income tax on US source compensation received for their services. The US source compensation is also subject to reporting and nonresident withholding under Section 1441. The US company compensating the director generally has the obligation to withhold and report the income. Failure to comply with withholding (if required) and reporting on Form 1042-S may result in a variety of penalties for the US company. In certain cases the US company may also have foreign reporting obligations as well.

Social security and residency issues

There may also be social security issues to consider for US directors of foreign companies which in some cases can be mitigated under a social security (totalization) agreement.

In addition, an unexpected and potentially adverse tax result may occur where a non-US company conducts its director meetings outside the jurisdiction in which the entity is located. In many countries, this may give rise to the entity having a tax residence elsewhere if that residency depends on the entity's place of management and not solely on its place of incorporation. This may potentially result in other tax filings and liabilities.

Actions to consider

Companies should review the status of directors on the boards of companies not resident in the countries where the directors reside. They may develop a process of tracking director meetings and activities to determine any portion of directors' fees earned in another country.

In addition, treaties should be reviewed to determine whether any exemption or modification of taxable income is applicable and ensure completion of appropriate documentation (e.g., US Form W-8BEN) to validate the foreign status of directors.

Let's talk

For more information about these issues, please contact your PwC Global Mobility Services engagement team or one of the following professionals:

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