The implications and challenges of non-compliance in Global Mobility **and how to avoid them**

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The management of compliance has always been an issue when assigning people internationally. The challenge is to ensure that tax, social security, and immigration legislation in both the home location of the employee, and the location in which they will be working are adhered to. And delivering the most cost effective and timely solution possible for the employer at the same time as achieving compliance, is always the goal to strive for.

This challenge has become more difficult in the last five years or so, for the following six reasons:

1. Whilst there are still large numbers of "traditional expatriates" (employees assigned to a foreign location for say, three years), there has been a rapid increase in the use of more "**flexible**" solutions such as, short-term assignments, cross-border or commuter assignments, or the frequent business traveler.

   This has been driven by a need for perceived cost-containment in the company, and employee reluctance to **accept longer term arrangements for family reasons such as spousal income or children's education**. These employees have been referred to as "**stealth**" assignees by some relocation professionals, as they are often not advised to Human Resources, and work **outside of any defined policy or compliance guidelines and procedures.** However to the **regulatory authorities the issues may be the same as for a longer term assignment.**

2. Multinational companies are now much more likely to be looking at their global workforce, and transferring different nationalities, than in the past when many staff came from the headquarters country. This means that the possible combinations of departure and destination countries, and thus the regulations that need to be understood and adhered to, are multiplied.

3. The increased threat of "global terrorism" and outbreaks of epidemics (for example SARS), have forced Governments to become more **restrictive regarding entry across their borders**, and to increase enforcement action regarding non-compliance. This has also meant frequent, and often rapidly introduced changes in procedures to apply for legal immigration status.

4. The increased use of technology such as e-mail, and the growth in business travel means that expectations of time-scales for delivery are more rapid than in the past. This gives Human Resources staff insufficient time to educate themselves in these complex areas. For the regulatory authorities it has meant greater co-operation both internationally, and domestically (for example, between immigration institutions and Revenue institutions) to enforce compliance.

5. Financial scandals such as **Enron** have brought greater attention to corporate governance in commercial day to day business

6. Many employers have reduced staffing levels in their Human Resource Departments requiring generalists to become involved in specialist activities

Even companies that manage all of their international assignment administration in-house will **often outsource compliance aspects** to specialist firms because of the complex nature of the ever-changing requirements. These companies however often understand the risks, at least in principle if not in detail.

However, Companies embarking into the international HR arena for the first time, or making use only of the "flexible" assignment types above, may be unaware of many of the requirements – **this is not a defence in terms of the law!**

Given that the compliance requirements are specific to each country, in an article of this nature we can only cover the main issues and common misconceptions/pitfalls in broad terms.

The implications of non-compliance

These are:-

- Where an employee, and/or his/her dependents enter, or attempt to enter, a country without the required paperwork, or with inappropriate or incomplete paperwork, this could mean **refusal at port of entry, or deportation.** For more serious breaches there might be **fines for the employee and/or the employer, and even imprisonment**
- Where tax is due on income under domestic legislation and this income is either not declared, or not paid in a timely manner, then there may be **potential tax penalties.** It is likely that the "missing" taxes and social charges will also have to be paid with interest. This could eventually lead to withdrawal of the work permit even if no immigration laws have been breached. The employer may be subject to similar penalties if they **fail to operate tax withholding and reporting obligations**
- Where the above is the case with a number of assignees in a country, then the company risks **being exposed publicly which could impact its ability to carry on business, and certainly would damage its reputation.** It would also mean that any future assignees from that Company are likely to be treated with unprecedented scrutiny.
- Exposure in this area may lead to audits into other areas of the business e.g. The corporate tax deductions it takes, or its internal accounting processes.

Whilst the diligence of Revenue authorities such as the Internal Revenue Service (IRS) in the United States is widely known, a number of other authorities have been high-profile in recent years in exposing non-compliance, for example India and Indonesia.

We will therefore now look at the main areas of compliance:-

1. Immigration

We will start with immigration as an employee should not enter another country unless he/she has the appropriate documentation to support what he/she is intending to do in that country, and it is that issue of "intent" that is the critical issue.

Nature of activity

The time spent in the country is not important, nor is the fact that the employee might remain employed and be remunerated in their home country, it is the nature of the activity that determines **whether and what type of visa/work permit** is necessary.

Whilst each country will have its own immigration laws and types of visa, there will normally be a type of visa that covers "business" and a visa or work permit that covers "employment".

On occasion there may be a "**waiver**" for a set time period, for example 90 days. Again each country will define what is meant by each term, but broadly a business visa would cover business negotiations, finalising a transaction or business agreement, or attending seminars, conferences and meetings.

For anyone involved in gainful economic or productive activity, an employment visa/work permit will be required. Only those that have full employment visa status should be paid by any overseas entity, as other than reimbursement of subsistence expenditure, this will **usually not be allowed under a business visa.**

It is for this reason that those on "flexible" or short-term arrangements may not be in compliance, as they often enter on a "business visa" in the mistaken belief that because of the short term, or irregular nature of their assignment, that is all they need.

Employees who regularly travel to one foreign location (even if any visa they hold allows multiple entry) are likely to come under closer examination each time they re-enter, as the immigration officials analyse whether the nature of their frequent visits is becoming closer to employment activity than what their visa may be intended for.

Human Resources staff should also be alert to those individuals who enter a country in full compliance with regulations on a "business trip" but who then get extended because the commercial considerations change. Often their visa status is not reconsidered.

Maintaining immigration status

It should be noted that a work permit is for an individual to undertake a specified activity for a specified period for a specified employer. If any of these criteria changes **then a new application needs to be made.** An assignee is therefore not at liberty to change his/her employer. Employers need to have a tracking system to monitor the expiry dates of work permits as they are rarely indefinite, and where required renew them in good time, as extension could take some weeks. There may also be maximum periods allowed on certain classes of visas after which the individual has to seek permanent residence, or repatriate.

Family members and other issues

If the assignee requires immigration documentation, it is likely that his accompanying family members will too. Human Resources staff need to be aware that there may be complications, or even refusal of entry where the spouse is of a different nationality (and particularly if it is one on an immigration authorities "**watchlist**"), or the life partner is not a marital partner or is of the same sex. This would be a problem with Middle Eastern countries for example.

Human Resources staff also need to be aware that there may be **complications in securing documentation for those who have criminal records.**

Even after work authorisation has been sanctioned, there may still be a need to secure residence permits or register with municipal authorities/the police.

Effect on other relocation issues

Problems, or delays in securing full immigration documentation may lead to consequences in other parts of the relocation process. For example, customs clearance may not be given at the port of entry for the international shipment of an individual's personal effects, until this has been obtained.

2. Unwanted Corporate Implications

For many companies, both large and small, there is a desire to avoid expense, time and undoubtedly, considerable documentation, by seconding an employee to work in another country without actually setting up a legal entity, or a physical office location in that country. Such a proposal might also be tempting to a Company "**testing the water**" in a new market before potentially expanding there.

Whilst again detail will differ from country to country, an individual acting on behalf of his or her employer on a continual basis, and where such appears to be his primary employment, is likely to create a "permanent establishment" of that employer in the other country, **which thereby exposes it to corporation tax.**

This will be the case even when the Company has an affiliate in that country, if the employee **is not directly working for that affiliate.**

As with the immigration status, the exact nature of duties is likely to determine the likelihood of creating a corporate tax presence, but certainly the ability to conclude contracts would normally give rise to such.

It is therefore possible for the individual to be deemed a "**permanent establishment**", and their residential address to be deemed the workplace.

We have most often seen such situations arising within the European Economic Area (EEA). In the countries affiliated to the EEA there is freedom of employment in any EEA country for an EEA national, ie no work permit is necessary to commence working, but this means, unless specifically agreed otherwise that they are subject to the legislation of that country, including that relating to corporations.

Sometimes companies seek to avoid these complications by appointing an "independent agent".

However, if the authorities believe that such a person is actually working for one company (ie he/she is not economically independent), is receiving regular income from them, and takes orders from them, then irrespective of the terminology used, **they would see it as a substantive employment relationship.**

In addition to any corporate tax implications, there may also be a requirement to register with the **Central Bank**, or regulatory authority for their appropriate industry **before being allowed to trade legally in that country.**

3. The Short Term Tax Trap

As we have advised, there is a growing trend to shorter term assignments (generally defined as less than one year), or flexible approaches such as commuting.

One of the reasons for this has been cost containment. Whilst it is true that employers may certainly save costs in the provision of benefits such as accommodation, the tax consequences are often not considered, or misunderstood, and this can lead to the savings being less than anticipated.

Employers also tend to believe that such arrangements are simpler. In fact from a tax perspective the challenge for professional advisers is to deliver the message that they are actually more complex!

There are a number of reasons for this:-

- Firstly, where an employee returns home regularly (e.g. commuter assignments) or is away less than twelve months, then they are unlikely to break tax residence in their home country, meaning that they will remain taxable on all income (unless exemptions exist on certain items), even on income that has not been paid in their home country.
- Generally, presence in a country for less than 30 days in a tax year will not give rise to a liability under the domestic law of most tax jurisdictions, unless those services are cross-charged, but presence above that should be examined.
- There is a common misconception that if an assignment to another country lasts for less than six months or 183 days in aggregate, then there is no tax liability. This is only true if there is a tax treaty between the two countries, (which overrides the domestic law) and certain other conditions within that treaty are fulfilled. The day count test is only one of three conditions to be fulfilled to gain exemption from tax in the assignment country. The other two are that the employee must continue to be paid by, or on behalf of an employer who is not a resident of the assignment country, **and the costs are not recharged to the overseas entity.**

All three conditions **must be fulfilled in order to achieve exemption**. It is the cost recharge aspect which is often forgotten, and sometimes Human Resources staff who are aware of the treaty requirements will not be aware of where the costs will be borne for a particular assignment!

Where it is known the assignment will exceed 183 days from the outset, or costs are to be recharged, then total exemption is not available.

If treaty exemption is originally applicable but then the assignment is extended so that 183 days is breached, the whole period becomes taxable not just the excess. Duration of assignments such as these **must therefore be very carefully monitored once set up.**

Please note that time periods in treaties may occasionally be less than 183 days, and may be based on any twelve month period rather than a calendar year.

The individual may then be taxable in both jurisdictions on the same income. Relief will usually be available , most often in the form of a tax credit, but overall the assignee will pay in aggregate the higher of the two tax amounts calculated under each domestic legislation, which may be more than was due at home. Alternatively, in some jurisdictions, exemption will be allowed in the home country for the employment income taxed abroad, but "exemption with progression" will apply.

This means that whilst the exempted income will not be taxed, it will be taken into account in determining the effective tax rate on any other income taxable in the home country.

4. Longer Term Tax Implications

By comparison those employees relocating for "longer" periods should be easier to deal with from a tax perspective.

Under a number of tax regimes, presence outside of the home country for a defined period will usually result in them successfully "breaking residence" **which means that the employer only need be concerned with the overseas tax.** However, a number of jurisdictions such as Canada, do not have a defined time period criteria for breaking residence, but use a number of factors to analyse whether an individual has moved his "centre of economic interests" elsewhere.

In these situations the risk is that the employer and employee assume that tax residence at home will be broken and structure the assignment remuneration to take into account host taxation only. If accommodation is retained, or the family do not accompany on assignment then this may not be the case.

Another common compliance issue is where the assignee is not paid wholly or at all in the host country. The location of the payroll is not a factor in determining the liability to tax. In jurisdictions which tax on a "worldwide income" basis then all income wherever paid is taxable. If the jurisdiction taxes on "source income" only, then it will tax on income relating to services performed in that country or income remitted to or recharged to that country, irrespective of where the income might actually be paid.

Split payrolls in such cases might be used for legitimate tax planning to reduce tax exposure in that country, but often such payrolls cannot be justified in this way, and therefore represent a compliance exposure if tax is not being properly declared.

Finally where assignees are not paid wholly in the host country, then the employer may still be subject to a requirement to withhold and pay across tax on a monthly basis to the host tax authorities on the income paid outside the host country. There is also likely to be a requirement to declare benefits outside of the overseas location as well e.g. home country retirement scheme.

5. Social Security

Social security is normally due on income earned in the host country to the host scheme. Often by reciprocal or totalisation agreements between countries, it is possible to gain exemption from this requirement and remain in the home scheme. Whilst this is well understood by companies operating internationally, **the compliance issues often arise in assessing what contributions are collected on.**

Many continue to base the contribution on what would be paid to the employee in the home country, and not the correct treatment, which for most schemes would be to base it on the assignment remuneration. **This is often higher than the equivalent home salary meaning that companies may be exposed to a deficit.**

How to manage compliance?

How can you avoid these problems:-

- Work with professional companies with extensive international experience of these issues. This will incur fees, but these will be less than the potential costs of non-compliance, **and should smooth the process of relocation.**
- Emphasize via written communication to line managers the importance of advising to Human Resources details of those who travel regularly, not just those on formal international assignment programmes. Where possible advise before such travel commences.
- Develop **policies to set out guidelines** for different types of assignment
- Set up systems to monitor employee travel and expenses, so that potential tax/visa issues can **be more easily identified.**
- International mobility of staff can be expensive, **but non-compliance can be even more expensive!**

IPM Global Mobility provides support and solutions for all the challenges listed in this guide — and more. So remember: when you need help, we're ready to give you a hand. Let us hear from you! Good luck with your international assignments program.

IPM Global Mobility team.

About IPM Global Mobility

If you are faced with managing your Mobility Programme, or are grappling with the technical problems, or associated compliance issues, you should consider outsourcing to specialists like us.

We provide comprehensive relocation support services to a wide range of clients and their assignees including those expanding operations to overseas locations for the first time, those experiencing a surge in global mobility from emerging markets, through to multinationals with an established global workforce.

Questions? Get in touch!

We are always here to inspire and help, so don't hesitate to contact us if you run into any problems or have any questions along the way of your international assignment programme.

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