Global Immigration and Mobility Handbook

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The Global Employer



**This content was last updated July 2021.**

Focus on Global Immigration and Mobility

Welcome to our go-to resource for in-house counsel, human resource managers and global relocation professionals to identify key mobility issues, ranging from business immigration and employment, to compensation and tax. Using the drop-down, select one of over 40 jurisdictions for vital information multinational employers need to know about managing the movement of managers and professionals, trainees and business visitors from short trips to long-term assignments.

To learn more about Baker McKenzie's Global Immigration & Mobility Practice, click [**here**](https://www.bakermckenzie.com/en/expertise/areasofpractice/global-immigration--mobility). Questions?

[**Contact us**](mailto:Debra.Pearlman@bakermckenzie.com)

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To subscribe to our full range of Employment and Compensation developments direct to your inbox, complete our [**online publications form**](https://bakerxchange.com/s/b52275c8bc7bb1e3d127c193dfe947efb93ddfba).

Editor's note

On behalf of Baker McKenzie’s Global Immigration and Mobility practice group, I am thrilled to share with you the newest edition of The Global Employer: Focus on Global Immigration and Mobility. This handbook is a product of the efforts of numerous lawyers throughout Baker McKenzie and selected local professionals at other firms.

With more than 150 immigration professionals in over 40 countries, Baker McKenzie’s Global Immigration and Mobility practice group is uniquely positioned to provide a full suite of legal services to clients. This handbook, which provides an overview of the business and legal considerations associated with global mobility assignments, is one of the many valuable resources made available to multinational companies that move employees around the world. The product of over 70 years of experience, the information found on the following pages is tailored to the feedback we have received from our clients who move employees globally.

We are thankful for this input and invite you to let us know what we can do to make this tool more useful to you and your colleagues.

### Related Content

Global Immigration Mobility Services



**Our global client care model** includes timely alerts on major changes in global mobility, immigration law and practice, a quarterly newsletter outlining global developments, and regular seminars and workshops on a broad range of issues:

**Workplace compliance**, including counseling, trainings, audits and litigation defense related to worksite enforcement and related employer initiatives

**Advocacy** on legislative reforms and regulatory changes, and agency practices around the world

**Design and implementation** of programs to accept immigrant investors, and schools and training programs to accept foreign students

**Coordination** among members of our global team to obtain visas, residence and work permits from consular offices or to execute transfers to the countries where you do business

**Transfers of staff** to existing and new multinational operations, including employees with specialist and technical skills, executives and managers and new employees hired from overseas

**Large-scale transfers**, including managing the immigration consequences of reorganizations, mergers, acquisitions, RIFs, redundancies, and related restructuring

**Transfer-related immigration matters**, including permanent residence, citizenship and relocation of spouses and other dependents

**Case management**, including maintaining employee records for visa renewals, provision of status reports, and planning and coordination of global immigration requirements

**Employment, employee benefits and tax advice** in relation to the transfer of staff, including structuring and auditing the employment relationship to ensure compliance with legal and tax obligations and to prevent obligations to prevent unauthorized employment

**Ancillary transfer issues**, working with a range of professionals in relation to shipping of personal belongings and customs and excise duties

**Establishment of new business operations abroad**, including the transfer of senior personnel to establish operations and related corporate and securities and taxation advice

Further Information

[**Baker McKenzie’s Global Immigration & Mobility Practice:**](https://www.bakermckenzie.com/en/expertise/areasofpractice/global-immigration--mobility)learn more about our market leading immigration and mobility practice and review the latest resources for global mobility professionals to mobilize talent.

[**The Global Employer: Global Immigration and Mobility Quarterly Update**](https://bakerxchange.com/rv/ff007b980790db827569dcb171459e03a3fc47b8) is a quarterly publication focused on the latest legal updates affecting global employee mobility.

[**The Accidental Expat: The Mobile Modern Workforce**](https://www.bakermckenzie.com/-/media/files/insight/publications/2019/01/bakermckenzie_accidental_expat.pdf?la=en) offers best practices for managing frequent cross-border travelers in your international organization.

[**The Global Employer: Focus on Global Immigration & Mobility**](https://www.bakermckenzie.com/en/insight/publications/2017/09/focus-on-global-immigration-and-mobility) provides employment-based immigration requirements for 35+ countries and more.

[**The Global Employer: Focus on US Immigration & Mobility**](https://www.bakermckenzie.com/en/insight/publications/guides/global-employer-focus-us-business-immigration) is a desk-side guide of employer obligations related to the movement of foreign nationals under US immigration and employment law.

[**Global Mobility Video Series**](https://www.bakermckenzie.com/en/insight/publications/2018/11/global-mobility-minute) offers easy-to-digest videos discussing key issues relevant to the management of a global workforce.

Your Roadmap to Hybrid Work provides resources to make it easy for US multinational employers to keep abreast of the most current legal changes during these challenging times.

Introduction



The global movement of employees is essential to multinational organizations doing business in different countries. Getting the right people to the right places at the right time with proper support in a lawful manner is critical to the success of global businesses. Human resources professionals and corporate counsel are confronted with a maze of legal issues that must be considered before moving employees across borders.

When can they go? How long can they stay? What can they do while there? How can they be paid? What happens to their employment benefits during the trip? Who will be the employer while abroad? Which country’s laws will apply? What are the tax consequences to the employer and the employee? What are the employer’s responsibilities for accompanying family members?

These issues confront employers dealing with both short-term business travelers, as well as employees on long-term assignments. This is a global mobility handbook to help guide you through the process.

The Global Employer: Focus on Global Immigration and Mobility

The next section of this handbook identifies the key global immigration and mobility issues to consider, regardless of the destination countries involved. Although the issues are inevitably intertwined, the chapters separately deal with immigration, employment, compensation and employee benefits, income taxes and social insurance, and global equity compensation. The final section is organized by country. For each country, this handbook provides an executive summary, identifies key government agencies, and explains current trends before going into detail on visas appropriate for short-term business travel, training, and employment assignments. Other comments of interest to global human resources staff are also provided.

Global Labor, Employment and Employee Benefits

There is often a gap between business necessity and practical reality when it comes to moving executives and other personnel to new countries. Employers must anticipate and deal effectively with a host of interconnected legal issues and individual concerns.

Baker McKenzie offers comprehensive legal advice related to global immigration — delivered locally around the world. We help employers plan and implement global transfers and provide on-site legal support to companies and employees in most major business communities around the globe.

Our network of Global Immigration, Employment, International Executive Mobility, Global Equity Services, and other lawyers in a variety of additional disciplines (e.g., tax and corporate) can assist you both pre- and post-transfer to ensure that:

Employment structures and contracts are properly documented and enforceable.

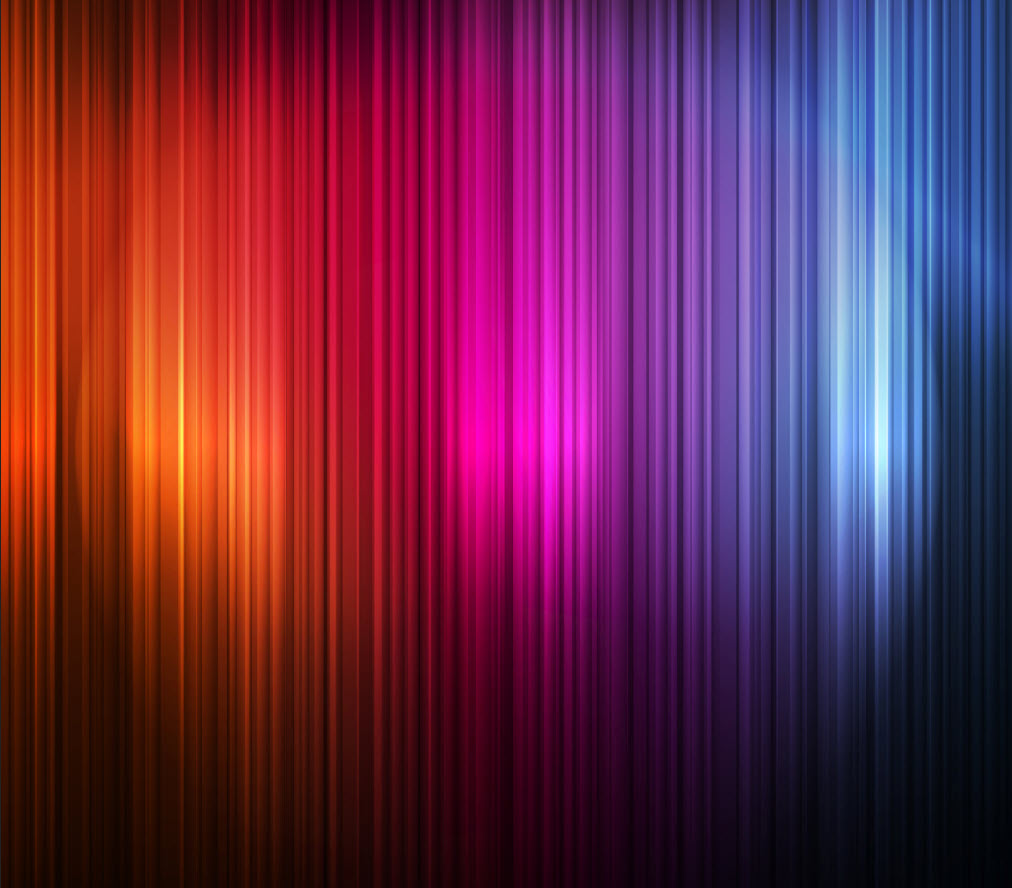
Employee benefits meet both the employee’s and the employer’s needs and comply with all relevant legal requirements.

Tax planning is sound and defensible.

Baker McKenzie has the unique ability to develop and implement comprehensive global immigration strategies and solutions to address the many needs of moving your employees globally.

Our knowledgeable professionals are qualified and experienced in the countries where you do business.

Immigration



Immigration laws vary from country to country. Although the specific names for visas and the associated requirements differ, there are common patterns and trends — especially for countries balancing the interest of engaging in global commerce against protecting local labor markets and national security.

Treaties and bi-lateral agreements often give special privileges to citizens from specific countries (e.g., benefits for European Union and European Economic Area citizens within the EU/EEA region and benefits for citizens of Canada, Mexico and the United States under the North American Free Trade Agreement). Be careful not to overlook these sometimes hidden gems when considering alternative visa strategies.

This chapter identifies the common patterns and trends. More specific country-by-country information can be found in the Country Guide Section.

Current Trends

It invariably takes longer than expected to secure all of the authorizations required before an employee can travel abroad for business.

The best laid plans often go away. Sometimes short-term business travel is the only way to meet an immediate need, however, the visas that are quickly available for such trips are generally not intended for productive work or long-term assignments.

In the interest of national security, and with concerns of protecting local workers, many countries are more actively enforcing prohibitions against unlawful employment. Penalties against employers are as common as penalties against foreign national employees. These penalties are increasingly including criminal punishments, rather than just civil punishments. Employers should obey both the spirit and letter of the law in this area, as failure to do so may damage an employer’s reputation with government agencies, impact the employer’s future visa requests and potentially result in potentially bad publicity.

With these points in mind, the employer should plan ahead and not rely on what may have seemed like quick solutions in the past. The use of tourist visas for business travel is not a solution. Problems only increase when family members accompany the employee on a holiday visa and then attempt to enroll children in local schools, or obtain a local driver’s license. Shipping of household possessions and pets is also ill-advised at this stage. Many countries will ultimately require the foreign national to depart and apply for the proper visa at a consular post outside the country — often in the country where the foreign national last resided or their country of nationality.

Business Travel

**Visitor Visas**

Multinational corporations routinely send employees to visit colleagues and customers in different countries. How easily this can be accomplished often depends as much on the passport carried by the employee, as does the country being visited. The length of the trip and the scope of activities undertaken can be key, with visa solutions for short trips under 90 days generally more readily available.

Travel for tourism and travel for short-term business visits are often authorized by the same visa, although, it is generally only true when the scope of the intended business activity does not rise to the level of productive employment in the country being visited.

Sourcing compensation locally during the visit is routinely prohibited, but the focus usually extends beyond the duration of the trip or the source of wages. Visiting clients, attending meetings and negotiating contracts are commonly permitted. Providing training and handling installation or post-sales service are commonly prohibited.

**Visa Waiver**

Many countries have provisions that waive the normal visa requirement for tourists and short-term business visitors. These visa waiver benefits tend to be reciprocal and are limited to citizens of specific countries (i.e., those that extend similar benefits to local citizens). Additional requirements (e.g., departure tickets) are sometimes imposed. Furthermore, the countries that enjoy visa waiver privileges frequently change, making it important to check for updated information with a country’s consular post before making travel arrangements.

Training

Employers with experienced staff in one country invariably want to bring newer staff from abroad for training. This is especially true when the research and development work happens in one country, the manufacturing is undertaken in another, post-sales installation and support are handled by regional centers, and the ultimate users are spread around the world.

Many countries offer specific visas designed for training assignments (e.g., Brazil and Japan). Some of these authorize on-the-job training that involves productive work. Others are limited to classroom-type and observation training and limit or prohibit productive work. Visas designed for employment assignments can often be used in training situations, if on-the-job training involving productive work is desired and not otherwise permitted by a pure training visa.

**Employment Assignments**

Visas for employment assignments are invariably authorized, however, the specific requirements vary widely.

**Work Permits**

Most countries are keen to protect their local labor market. A recurring solution is to impose some kind of labor market check or test as a prerequisite to issuing a visa for an employment assignment (e.g., Malaysia). These are often handled by a Ministry of Labor or equivalent government labor agency which is distinct from the Foreign Affairs governmental agency that issues visas at consular posts. In many countries, the labor agency’s authority is framed in the context of a work permit.

A work permit, or equivalent document, is generally required for employment assignments. However, it is also common for countries to have visas that are exempted from the work permit requirement (e.g., Belgium). The number of exemptions greatly exceeds the general rule.

Who is exempted depends on the country. Most countries exempt employees that are transferred within multinational companies, business investors and high-level/key employees.

Education, especially higher level education in sought after fields, can often be used to qualify for employment assignments. Academic transcripts showing completed studies are frequently required and letters verifying employment experience can be similarly useful.

**Residence Permits**

Concern over national security is becoming increasingly common. Background clearance checks and the collection of biometric data for identification purposes is common today. A number of countries have already addressed this concern by instituting a reporting and registration requirement. This reporting requirement can be satisfied in the form of a residence permit, usually handled by a Ministry of Justice, Ministry of Interior or an equivalent agency. In other cases, or in combination with the requirement above, employees must report to local police authorities upon arrival into the country (e.g., France and Italy). These requirements are equally as important to maintain the status to lawfully live and work abroad as obtaining the proper visa.

**Other Concerns**

An increasing number of countries are requiring medical or physical examinations, aimed at limiting the spread of contagious diseases (e.g., Saudi Arabia, People’s Republic of China and Russian Federation).

Most countries offer derivative visa benefits to accompanying family members, however, what constitutes a family member varies across jurisdictions. Family members often include spouses and unmarried, minor children. An increasing, but still minority, number of countries offer derivative benefits to different-sex life partners while other countries also extend these benefits to same-sex partners (e.g., Canada and the Netherlands). Some countries consider family members to include more distant relatives (e.g., parents in Colombia) and older offspring, generally if such relatives are dependents of the principal visa applicant’s household.

Generally, documents submitted in support of the immigration process need to be translated into the local language. Many countries require that public documents (e.g., articles of incorporation, company registration, birth certificate and marriage certificate) be authenticated by attaching an internationally recognized form of authentication or “apostille” (e.g., Spain). This cumbersome process usually involves the following steps:

First obtaining an authentic copy of the document from the pertinent government agency that retains the official record.

Second, sending that document to the government agency responsible for verifying the authenticity of that document.

Lastly, certain countries also require consular legalization of the authenticated document (e.g., Brazil and Italy).

**Further Information**

See the Country Guide Section of this publication for more specific information regarding specific country’s visa requirements. Please contact your Baker McKenzie attorney for specific guidance on current legal requirements and how they apply to your company’s needs.

Employment



Integral to mobility planning is identifying and establishing the appropriate employment structure for an employee being sent to work in another jurisdiction. For planning purposes, it is important to keep in mind the laws of the jurisdictions involved, the business goals related to the foreign assignment and the individual’s situation.

Employment Structures for International Transfers

The primary question to ask is, who will be the employer? That is, who will have the right to direct and control the activities of the employee while working abroad? In general, multinational companies typically use one of the five following employment structures to answer this question:

Secondment – the employee remains employed by the home country employer and is loaned or seconded to work for an entity in the host country.

Secondment “Plus” – a hybrid structure combining “Secondment” and “Dual Employment” in which the secondment structure has been chosen and the employee remains employed by the home country employer, but the host country also requires direct employment by a local entity for immigration, tax or employment purposes.

Transfer of Employment – the employee is terminated by the home country employer and is rehired by a new employer in the host country.

Global Employment Company – the employee is terminated by the home country employer and transferred to the employment of a global employment company (GEC). In turn, the GEC seconds the employee to work for an entity in a host country.

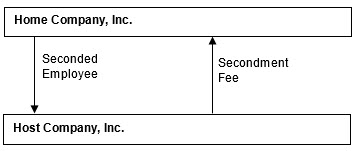
Dual Employment – the employee simultaneously maintains more than one active employment relationship during the course of the assignment (the employee works for two or more employers).

In addition to these five main structures, multinational companies sometimes use other, less-popular structures. For example, in several European countries it is possible to use a “dormant contract” approach whereby the employee’s existing employment relationship is suspended for the duration of the foreign assignment, the employee is formally transferred to and becomes an employee of another company for the duration of the assignment and then the employee’s dormant contract is “revived” upon termination of the assignment and the employee’s return to the original employer. In some jurisdictions, which impose restrictions on the use of fixed term employment arrangements, this approach creates a risk of an indefinite term employment relationship with the new employing company even though the employment is structured as a fixed term arrangement for the assignment period. Other possible structures include commuters, extended business travelers, putting the employee on a “leave of absence” for the duration of the assignment or terminating the employee and then re-hiring the employee as an independent contractor.

Secondment

In the typical secondment scenario, the employee remains an employee of the home country employer (Home Company) and is sent to the foreign jurisdiction to provide services for the benefit of the host country employer (Host Company). Secondments under this scenario are sometimes referred to as “assignments” by some companies, although in principle the term “assignment” can refer to any period of time the expatriate works outside of the home country under any employment structure.

**Typical Secondment Structure**



The employee continues under the home country employment contract, except to the extent modified by the terms of the employee’s letter of assignment and duties in the host country. In exchange for receiving the services of the seconded employee, the Host Company typically pays a fee to the Home Company – usually equal to the costs of compensating the seconded employee and sending him on secondment. Sometimes there is a profit mark-up on the secondment fee, as determined in consultation with tax advisors and based on transfer pricing principles.

In documenting a secondment, great effort should be taken to expressly continue the Home Company employment relationship (and especially the “at-will” status of the employee when the home country is the United States, for example) so as to provide a contractual argument against the application of host country termination protections and entitlements. However, as a practical matter, it is likely that an employee working in a host country will be eligible for the benefits of the employment laws of the host country during the course of the secondment and upon termination.

Assignment letters for secondments typically include the following provisions:

confirmation that the employee remains employed by the Home Company (e.g., at-will status for US outbound secondees)

details of the role, reporting relationship and anticipated duration of the assignment

details on salary and benefits, including specific expat benefits such as housing allowances, relocation expense reimbursement or cost of living differential

tax equalization/protection language where applicable, or language requiring the employee to be responsible for any additional tax triggered by the secondment

compliance language (such as compliance with the US Foreign Corrupt Practices Act)

provisions addressing what happens upon termination of the assignment and also upon termination of employment

anti “double dip” language, preventing the expat from enjoying benefits under the laws of both the home and host jurisdictions (e.g., severance pay under the laws of both home and host jurisdictions in the event of termination)

choice of law and choice of forum provisions (which could be very important in the event of a dispute with the expatriate over the terms or benefits under the secondment)

compliance with data privacy laws

compliance with immigration obligations in the home and host countries and whether the company will assist with the arrangements

Another concern created by use of the secondment approach is the potential permanent establishment (PE)/ taxable presence issue created if an employee of one country is sent to work in another. Since an employee is deemed to be an extension of their employer, the mere presence of an employee in a foreign country allows the host country to tax the Home Company. To mitigate the corporate tax risks for the Home Company associated with PE, the assignment letter should expressly provide that the individual does not have the authority to conclude contracts on behalf of the Home Company while on secondment. In many cases, this covenant will be extremely helpful to defeat a PE in situations where the employee is seconded to a host country that has an income tax treaty with the home country. Consultation with tax counsel about this issue is recommended given that there are exceptions. Note that in the case of secondments to certain jurisdictions (e.g., Canada, China and India) the covenant not to conclude contracts will unfortunately not be sufficient by itself to mitigate the PE risk.

Secondments remain the most common employment structure for expatriates. Secondment is particularly desirable where the employee wishes to remain in home country employee benefit plans, such as a retirement or pension plan, while working in the host country. For example, many US expatriates like to remain covered by their US-tax qualified retirement plans and other US benefits while working abroad. As such, the secondment structure facilitates this extended participation. See the chapter “Compensation and Employee Benefits.”

Secondment “Plus”

A common issue presented by the typical secondment structure is that it will sometimes be challenging to implement where the employee –as a matter of local employment, immigration or tax law (or as a matter of common practice) – is required to be employed by a local entity to work in the host country. For example, it may be a condition precedent that the employee execute an employment contract with the Host Company to receive proper immigration papers and a work permit to enter the host country. This has become very common in Latin American, Middle Eastern and African jurisdictions (e.g., Argentina, Brazil, Colombia, Bahrain Saudi Arabia, the UAE, Algeria, Angola and Equatorial Guinea) and is also a growing trend in certain European and Asia Pacific jurisdictions (e.g., Denmark, Russia, China, Indonesia, South Korea and Vietnam). Furthermore, in some countries, an individual with a certain title (e.g., CEO) must be employed by a local entity in that jurisdiction as a matter of local employment law.

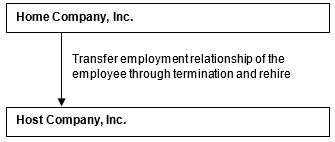
Notwithstanding the local legal requirement for the individual to be employed locally by the Host Company to work in the host jurisdiction, it is possible to combine the secondment approach with local law employment requirements and still preserve the benefits of the secondment approach. This works in situations where the individual can be considered an employee of the Home Company for home country purposes, and an employee of the Host Company for host country purposes. The Home Company employment governs the terms and conditions of the assignment, and the assignment letter directs the individual to enter into an employment relationship with the Host Company to meet the legal requirements of the host country. In some cases, a written employment contract with the Host Company can be streamlined by including only the terms and conditions strictly required by law, however, it may not be required if it is sufficient to reflect in the assignment letter that the Host Company will supervise the activities of the individual while working in the host country.

Transfer of Employment

In the transfer of employment structure, the employee’s employment with the Home Company is terminated and the employee is rehired by the Host Company. This structure is the preferred approach from an employment law perspective as it creates a “clean break” between employing entities, and thus provides clarity as to what laws govern the employment relationship going forward. It also avoids the risk of a PE issue, since the employee will always be employed, i.e., directed and controlled, by the Host Company.

As this structure involves a technical termination of employment, all termination-related obligations and payments are triggered (e.g., severance pay, termination indemnities, distribution of accrued pension benefits, the final paycheck and vacation payout). While many multinationals handle this issue by asking the employee to waive their entitlement to these benefits, in some jurisdictions the payment of severance upon termination of employment is mandatory, even if the employee is to be rehired by a related company, and cannot be waived as a matter of local law and public policy. This risk can often be mitigated by including appropriate “offset” language in the assignment documentation (similar to the anti “double dip” language referenced earlier). Another issue to consider is that a transfer of employment requires the employee to start as a “new hire” with the new employer, which may mean the loss of seniority and credits for prior years of service with the former employer (unless the new employer agrees to maintain such seniority and service credits). Furthermore, at the end of the assignment when the employee returns to the Home Company, the employee will again have to be terminated and rehired, which will again trigger severance payments and obligations as before. Thus, while it is the preferred approach for certain reasons, this approach is also typically the most expensive and administratively burdensome for the employer to implement.

**Typical Transfer of Employment Structure**



Documenting a transfer of employment is usually a two-step process. The first step is a letter agreement between the current employer and the employee to terminate the employment relationship, and for the employee to waive any notice or severance entitlements (vacation rollovers also can be addressed) if allowable in the particular jurisdiction and in accordance with local laws. The letter agreement also presents an opportunity to obtain a release of claims (if allowable under local law) from the employee if there are any potential concerns regarding latent claims against the Home Company.

The second step is an offer letter or employment agreement with the new employer. As the employee in this situation has a history with the Home Company, it is common practice to not include any probationary periods in the new offer of employment and, where permitted or desired, to recognize prior service with the Home Company for the purposes of participating in employee benefit plans with the Host Company and other seniority purposes.

Where all the parties are amenable to the transfer, this transfer of employment is frequently documented by executing a tripartite agreement between the Home Company, Host Company and the employee which documents the mutual termination with the Home Company and rehire by the Host Company and clearly outlines the employee’s entitlements as part of the process. A new employment agreement or offer letter from the Host Company is then attached to the tripartite agreement.

Multinational companies often tend to use this employment structure for long-term or permanent assignments to a new jurisdiction. For short term assignments, termination and rehire is not the first choice.

Global Employment Company (GEC)

This structure is something of a hybrid – combining elements from both the secondment and transfer of employment structures. First, the employee is terminated by the Home Company and rehired by a global employment company (usually an affiliate) organized for the express purpose of employing expatriates for the GEC. The GEC, as the employee’s employer, becomes the employee’s new Home Company and seconds the employee to work for an affiliate.

The use of a GEC can offer employers the opportunity to create a uniform structure for their global mobility program. All expatriates would be under one “umbrella” as they would all have the same employer — the GEC. The GEC allows a multinational company to adopt a uniform approach to compensation, benefits, social security and income taxation for its global workforce. The GEC also provides an effective buffer for any PE issues that may arise, due to the GEC becoming the “employer” and therefore it is only the GEC that has PE exposure.

Multinational companies can look to a variety of jurisdictions as the location for their GEC. There is no one right choice in this regard and the choice of GEC jurisdiction is primarily a tax decision. It is common to set up a GEC either in a jurisdiction with a robust income tax treaty network (e.g., the Netherlands, Singapore or Ireland) or in a jurisdiction with minimal or no corporate income taxes (e.g., the Cayman Islands, Bermuda or Guernsey). Other considerations when selecting a GEC jurisdiction include:

whether the laws are employer-friendly

whether it is relatively easy to set up a new company in the GEC jurisdiction

whether local laws allow the GEC to be operated and managed from afar

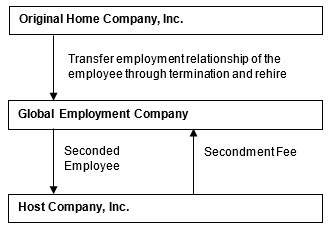
whether the company has other affiliates in or experience with the GEC jurisdiction

what substance requirements the potential GEC jurisdiction may have to operate the GEC on a daily basis

Depending on the size and variety of the expatriate population, a multinational may decide to set up multiple GECs for different regions, for different lines of business, or for different nationalities of expatriates (e.g., a US GEC for US citizen expatriates and a non-US GEC for all other expatriates).

The GEC is a real company established with all the corporate formalities as any other affiliate, i.e., with capital, a bank account, designated directors, a registered agent and often actual employees who work full- or part-time as GEC employees to manage its business. Sometimes, a GEC will be established as a “paper” company, meaning it exists as a real company, has capital, a bank account, designated directors, a registered agent, but it has few, if any employees. The employees that it would hire to help it manage its business are replaced with business services contracts (e.g., accounting, payroll, employee benefits and HR) with related companies. In exchange for these services, the GEC pays a service fee to the related companies, often with an arm’s length profit mark-up. In either case, the GEC receives income from secondment fees with affiliates who need the services of its expatriates, and then uses this income to pay its own employees to run its business, or to pay for the business services with related companies who provide those services to it. With the correct planning, there will be little or no profit left at the end of the year on which the GEC can be taxed.

**Typical Global Employment Company Structure**



GECs are popular with multinational companies with large expatriate populations. Given the amount of legal, corporate, tax and other work necessary to set up a GEC, companies with smaller expatriate populations tend not to use this alternative. Some industries tend to favor GECs more than others, for example, GECs are very popular in the oil and gas industry as these companies have historically sent lots of expatriates to work in other countries on temporary assignment. Special to this industry is a type of employee called a “rotator” (e.g., an employee who works 28 days in another country, followed by 28 days back home) for assignments lasting months or years. Rotators are important roles in connection with energy exploration and production in various jurisdictions all over the world, and some companies have hundreds or even thousands of rotators. In these instances, the GEC structure makes perfect sense.

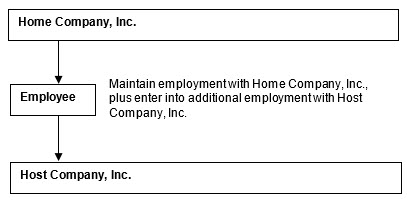
Dual Employment

In the dual employment structure, the employee has two active employment relationships — one with the Home Company and one with the Host Company.

A dual employment structure is often used in a situation where the employee provides separate and distinct services that benefit more than one entity, such as a sales manager who is selling products covering more than one line of business, or an executive who has multiple titles and reporting relationships in different jurisdictions across a region (e.g., reports to the corporate headquarters in one country but also has local management responsibility in another country). A dual employment structure is sometimes necessary where local employment is required for the expatriate to obtain a visa or work permit, but the expatriate wants to continue the employment relationship with his Home Country employer to continue participating in Home Country benefit plans. In that case, the compensation is often split between the two countries in proportion to the amount or type of work performed for each employer. In some countries, if the employee is classified as “exempt” for overtime purposes, care must be taken to ensure that the employee still receives sufficient compensation under both contracts to meet the exemption. In some cases, dual employment can achieve some favorable income tax results for the employee. For example, where an employee works both inside and outside of a host jurisdiction that taxes compensation on a remittance basis (e.g., the UK, Hong Kong and Singapore), only the compensation for work performed in the host jurisdiction is taxable by the host jurisdiction, provided the compensation is not paid or remitted to the employee in the host jurisdiction. There are very few countries where this type of employment structure can achieve these types of income tax results. Due to the complexity of a dual employment structure, careful planning is required to avoid paying the expatriate double their compensation, creating complex income tax results, or incurring fines and penalties for failing to withhold or report income where required.

This employment structure is more burdensome than the other structures as it requires maintaining two distinct employment relationships, two employment agreements, multiple tax and filing obligations, and has multiple payroll and benefits implications. As a result, it is the least common employment structure for expatriates.

Documenting a dual employment relationship usually involves a separate employment agreement for each employer. These agreements should be carefully drafted to appropriately document the duties, responsibilities, time allotment and compensation for each separate employment relationship, and to avoid paying the employee more than 100% of the compensation he is owed for providing services to both employers.



Further Information

The Global Employment and Compensation Law Practice works in coordination with the Global Immigration and Mobility Practice. Employment practitioners help structure employment relationships for global mobility assignments that factor in the employment laws of multiple countries/jurisdictions. They also assist multinational companies in developing corporate policies and practices for global mobility assignments, as well as guide employers on current trends and best practice solutions. They play a key role in pre- and post-acquisition integration on mergers, acquisitions and reorganizations, as well as redundancies and reductions in force.

Compensation and Employee Benefits



*Last updated April 2020.*

A major concern for both expatriates and their employers is what compensation and employee benefits will be provided to the expatriate while they are on assignment. While many multinational companies have compensation packages and employee benefit plans that are designed specifically to cover the expatriate population, this is not the case for all companies. Some companies attempt to keep the expatriates in the same benefit plans and insurance policies as their other, stay-at-home employees. In other cases, the employer has to customize compensation and employee benefits for one or several expatriates to fit their particular situation. In short, there is no universal practice among multinational companies. The factors that will influence the amount, type and design of the expatriate’s compensation and employee benefits package include:

the employment structure

the jurisdictions involved

the length of the expatriate’s assignment

the types of employee benefit plans currently provided by the employer

whether benefits coverage can be easily extended to the expatriate under the terms of the employee benefit plan; whether the expatriate will return home or go out on new assignments

Compensation and Payroll

The two primary elements of an expatriate’s compensation package are base salary and bonus opportunity. Understandably, there is no single approach or best practice for every case. Each expatriate situation is different, and how much the employer is willing to pay the expatriate in terms of base salary and bonus opportunity will depend largely on the employer’s compensation policy, the value of the expatriate to the business, the expatriate’s seniority and experience in the field, and other similar factors. Notwithstanding, in most cases the expatriate’s base salary on assignment will be no higher than their current base salary. Even if the assignment is deemed to involve more responsibility, employers are reluctant to increase base salary “just because” of the assignment and instead reflect any additional compensation in the form of bonus or expatriate allowances. Handling base salary in this manner avoids the problem that may occur when an employer temporarily increases base salary during the assignment, and then wants to reduce the level of base salary at the end of the assignment to the former level. Often, such “up and down” movement is not successful, as the expatriate wants to keep the base salary increase upon their return to the home country and make it permanent.

Once the employer has determined how much base salary and bonus to pay the employee, the next question will be: Where and how will the employee be paid?

In the case of a secondment, for example, it is common for the employer to provide that the expatriate will remain on their home country employer payroll, but may also be placed nominally on the payroll of the host country employer (a so-called “shadow payroll” or “phantom payroll”) so that local income taxes or social taxes can be remitted on behalf of the expatriate to the local tax authority. It is also common to split the pay of the expatriate on secondment, so that a portion of the compensation is paid locally to cover local taxes and expenses, while the bulk of the compensation is paid to the expatriate via direct deposit into the expatriate’s bank account in the home country.

With a few exceptions, there is no legal requirement regarding where the expatriate must be paid (that is, what payroll must cover the expatriate). More often than not, an expatriate can receive compensation in the host country, in the home country (e.g., direct deposit into a home country bank account that can be accessed in the host country) or a combination of the two. In some situations, however, local immigration or employment laws require that an expatriate working in the host country be paid from the local payroll, i.e., they must be paid in the currency of the host country by the host country employer. In other situations, it may be difficult for the expatriate to access any funds paid to them outside of the host country due to currency exchange controls, which makes a local payroll the only practical option.

Payroll by itself is typically not determinative of the employer-employee relationship. That is, a company does not become the expatriate’s “employer” merely because the expatriate is on its payroll. Often, an expatriate sent to a jurisdiction will be put on the local company payroll as an accommodation (for example, to facilitate the payment of local income tax and social insurance taxes). Alternatively, companies are sometimes designated to serve as payroll agents for other companies merely because they have an existing payroll function and personnel who are familiar with the local payroll requirements. For example, the host company might pay compensation to the expatriate as a “payroll agent” on behalf of the expatriate’s real employer in the home jurisdiction. Moreover, the home country employer might continue to cover the expatriate in the home country benefit plans, and might even continue to contribute to home country benefit plans on behalf of the expatriate, even though the expatriate is now employed by another company. Thus, the payroll location will not, by itself, be determinative of who the expatriate’s employer is.

Having said that, payroll is an important issue in connection with an expatriate assignment, since moving the expatriate to a new payroll must be handled successfully to maintain compliance with applicable reporting and withholding requirements.

Where compensation is delivered to the expatriate in the host jurisdiction, it will be subject to any applicable income tax and social tax withholdings, unless an exemption applies. Understanding local law is therefore critical to ensuring that the expatriate’s payroll is structured correctly and is compliant.

**Extending US Tax-Qualified Plans to Employees Working Abroad**

A common question is whether a US expatriate can continue to participate in a US tax-qualified retirement plan while working outside of the US on an international assignment.

A US tax-qualified retirement plan may provide certain US tax advantages that a foreign retirement plan cannot, such as:

a pre-tax contribution feature (e.g., plans under Section 401(k) of the US Internal Revenue Code of 1986, as amended (Code))

no current US income tax on the contributions made to the plan on the employee’s behalf

no current US income tax on earnings of the plan prior to distribution

favorable US income tax treatment upon distribution (e.g., tax-free rollover treatment)

A US expatriate may be reluctant to part with these tax benefits unless a substantial expatriation bonus or other “gross-up” allowance is offered. Further, the employee may not be able to accrue a meaningful retirement benefit from any non-US retirement plan if the employee’s assignment will be short. Moreover, even if the employee can accrue a sizeable benefit during the assignment, the contributions made to such a plan on the vesting or accrual of such benefits may be taxable under US income tax law. Alternatively, the benefit may be taxable under US income tax law upon distribution.

A US Tax-Qualified Retirement Plan Must Cover “Employees”

The plan sponsor should review the plan document and determine whether an employee working outside of the US can remain a participant in the plan. If not, the plan will need to be amended.

The most critical aspect for plan participation purposes is the employer-employee relationship. A US tax-qualified retirement plan must be limited to employees of the plan sponsor or any member of the plan sponsor’s controlled group. The plan may not cover individuals who are not “employees.” For these purposes, an individual is an “employee” if the individual’s employer has the right to direct and control the activities of the individual. Failure to limit plan participation to only employees may result in disqualification of the plan, which would mean that all participants’ vested benefits would become immediately taxable under the plan, even if they have not yet retired or become entitled to a distribution under the plan, among other things.

Accordingly, the employee will continue to participate in the retirement plan of the US employer if the employee is working for a US employer and is seconded to work for a non-US company because, in a secondment structure, an employee remains directed and controlled by their home company employer and, therefore, technically remains an employee of the US employer.

Furthermore, if the employee transfers to a foreign branch of a US employer, the employee can continue to participate in the US employer’s tax-qualified retirement plan because the foreign branch is merely an unincorporated association and is treated as an extension of the US employer.

However, with a few exceptions (described below), the employee would no longer be eligible for participation in the plan where the employee terminates employment with the US employer and is rehired by a non-US company that is outside of the plan sponsor’s controlled group. In that case, the employee’s participation in the plan will cease when employment is transferred.

Controlled Group Coverage

If an employee terminates employment with the US employer and is rehired by a non-US company, participation in a US tax-qualified retirement plan can be preserved if the non-US company is a member of the same controlled group as the plan sponsor. For these purposes, a “controlled group” is defined as a “controlled group of corporations,” or “trades or businesses under common control” under the Code.

A “controlled group of corporations” is either a parent-subsidiary group in which the parent owns at least 80% of the stock of the subsidiary, or a brother-sister group in which five or fewer individuals own at least 80% of the stock in two or more corporations, and at least 50% of such ownership is identical with respect to each corporation. Similar rules exist for “trades or businesses under common control” (which include unincorporated entities) and affiliated service groups.

For the purposes of US tax qualified retirement plans, controlled group rules include non-US entities in the definition of “controlled group,” despite the definition of an “affiliated group of corporations” eligible to file a US consolidated group income tax return technically excluding them.

The IRS has ruled that due to the application of the controlled group rules, employment is tested on an entity-wide basis. Employment with any one member of the controlled group will be considered to be employment sufficient to participate in the plan as an “employee.” An employee can continue to participate in the tax-qualified plan without disqualifying it, considering that they transfer employment to a member of the same controlled group. The plan document should be reviewed to confirm that participation can be extended in this manner.

Potential Loss of US Tax Deduction

If an employee’s participation can be continued because they are transferring employment from a plan sponsor to a foreign company that is a controlled group member, the plan sponsor is not automatically entitled to a US federal income tax deduction for its contributions made on behalf of such employee. The plan sponsor may only deduct contributions made on behalf of its own employees, therefore, the controlled group rules and the income tax deduction rules are not synchronized. Notwithstanding, the IRS has ruled in a private letter ruling that if the controlled group member adopts the plan for the benefit of the employee, the contribution made on behalf of an employee who works for the controlled group member is deductible by the plan sponsor, the same as if the employee remained employed by the plan sponsor. To preserve the ability to take a US federal income tax deduction for contributions made to the plan, the foreign employer would have to adopt the plan.

Non-deductible contributions would generally give rise to a special 10% excise tax payable by the employer. As long as the non-deductible amount contributed on behalf of the employee does not exceed the amount allowable as a deduction under Code Section 404 (e.g., 25% of compensation), then the 10% excise tax does not apply.

Treat Assignment as a “Leave of Absence”

If the employee will be working abroad on a temporary assignment, they may be able to remain a participant in the US tax-qualified retirement plan if the assignment is characterized as a “leave of absence.” The relevant Treasury Regulations provide that a US tax-qualified retirement plan may cover employees who are temporarily on leave. To use this approach, the employee would have to remain employed by the US plan sponsor as an inactive employee.

Working for a “Foreign Affiliate”

An employee’s participation in the US tax-qualified retirement plan can also be continued if the employee is employed by an entity in which an “American employer” (which includes a US corporation) has a 10% or more interest (for these purposes, a “foreign affiliate”). This provision is found in Section 406 of the Code, but is not commonly used since the application of the controlled group rules, described above, has lessened the attraction of this Code provision as a means to continue plan participation.

Where this provision is utilized, the employee of the foreign affiliate will be treated as “employed” by the American employer for the purposes of the American employer’s tax-qualified retirement plan (even though they are not really employed) if certain requirements are met:

The American employer agrees to extend US Social Security coverage to all of the foreign affiliate’s employees who are US citizens or residents by means of a Section 3121(l) agreement filed with the IRS.

The employee does not participate in a local funded, deferred compensation plan.

A similar provision applies to certain employees of US subsidiaries having non-US operations under Section 407 of the Code.

Adoption by Foreign Employer

Plan coverage could also be continued by arranging for the foreign employer to adopt and contribute to the plan. In that case, the plan would be deemed to be a “multiple-employer” plan, and would have to comply with additional participation, coverage, non-discrimination, reporting and other requirements to maintain tax-qualified status.

Foreign Law Implications

There are a number of foreign laws that may affect an employee’s continued participation in a US tax-qualified retirement plan while on foreign assignment, including the following:

*Tax Laws*. The employee might be immediately taxed under local rules on contributions or benefit accruals made on their behalf under the plan. The local tax rules may provide, for example, that plan benefits are taxable when accrued, when a contribution is made to the plan or allocated to a plan account on the employee’s behalf, or when the employee vests in the contribution.

*Labor Laws*. In certain countries, plan benefits or contributions may be subject to a works council consultation procedure before they can be offered to employees. While it is unlikely that works council approval or consultation would be required with respect to just one or two US expatriates working in a foreign country, if a larger group of employees are involved then it will be important to check with local labor counsel, especially in an EU jurisdiction, regarding the implications. Plan benefits may also have to be taken into account when determining the employee’s dismissal pay or termination or severance indemnities that may be payable when the employee leaves employment. Furthermore, the plan benefits may breach compliance with certain non-discrimination rules in the jurisdiction, particularly if there is a requirement that the expatriate’s compensation be no greater than a comparable employee who has been hired locally by the foreign company. There is also a risk in some “acquired rights” jurisdictions that plan participation and benefits may not be terminated or revised unilaterally by the employer without the employee’s consent.

*Securities Laws*. If employer stock is allocated to the employee’s account under the plan, foreign securities laws may require compliance with certain registration or prospectus distribution requirements, unless exemptions are applicable.

Coverage under Non-US Retirement Plans

Although there are many reasons why a US expatriate may prefer to remain a participant in a US tax-qualified plan, there are also a number of reasons why the expatriate may end up participating in a local retirement plan instead. For example, if the employee is hired by an employer outside of the controlled group, they may simply be unable to continue participation in the US plan. Alternatively, the US plan sponsor may not be able to, or may not want to, extend coverage to the expatriate.

Additionally, the local plan may provide more generous retirement benefits than the US plan. For example, in a number of European countries, private pension plans provide for a cost-of-living indexation of retirement benefits. This indexation means that retirement benefits are increased for cost-of-living adjustments each year, which results in a larger benefit to the retiree over time. US tax-qualified plans generally do not provide this enhancement.

Finally, local law may currently tax the employee on contributions, earnings and accruals if the employee participates in the US tax-qualified retirement plan while resident in the local jurisdiction, although the employee will not be taxed if they participate in a retirement plan in the local jurisdiction.

For these reasons, participation in a local retirement plan may be attractive to the expatriate. This result is even more likely if the US tax-qualified retirement plan does not penalize the employee for discontinued plan participation through lengthy vesting schedules, final pay benefit formulae or restrictive definitions of “compensation.”

Some representative, non-US retirement plans are described below.

In the UK, pension plans fall into two general categories: the State Pension and private pension schemes. The State Pension has undergone changes in its structure. It previously consisted of a basic (flat rate) State Pension and the Additional State Pension. Effective 6 April 2016, the State Pension is structured as a single-tier pension and is funded by mandatory social insurance contributions called “National Insurance Contributions” from employers and employees.

Most UK private pension schemes are set up by employers to supplement the State Pension, although an increasing number of individuals are establishing their own private arrangements and pensions. Employers, and in most cases employees, will finance the scheme through an irrevocable trust that will normally comply with certain statutory requirements, in the same manner as a tax-qualified retirement plan in the US must comply with the requirements of Code Section 401(a). If the scheme is approved by HMRC (the UK tax authorities), the contributions paid by the employer are deductible, the employees are not taxed on their employers’ contributions and any investment earnings of the fund are not subject to tax.

In Canada, there are several different kinds of private pension plans. These plans fall into two basic groups: registered plans and unregistered plans. In addition, the Canada Pension Plan provides mandatory social security benefits.

Registered Pension Plans, which provide for tax-deductible employer contributions, are generally either defined contribution plans or defined benefit plans that have been registered with the Canada Revenue Agency. Other types of registered plans include Deferred Profit Sharing Plans and Group Retirement Savings Plans (where one or more individual Registered Retirement Savings Plans are sponsored as a group plan by the employer).

Unregistered arrangements include a retirement allowance, which is a lump sum at retirement, and a Retirement Compensation Arrangement, under which employer contributions are made to a custodian and are subject to a 50% refundable tax. Pension plans may also be classified as Employee Profit Sharing Plans, Employee Benefit Plans or Salary Deferral Arrangements.

In Hong Kong, retirement schemes are regulated by the Occupational Retirement Schemes Ordinance (ORSO). Unless an exemption from registration applies, it is a criminal offense for an employer to operate, make a payment to, or otherwise contribute to or participate in, an unregistered scheme. However, the rights of members of unregistered schemes are protected.

ORSO requires a scheme to be registered if it has or is capable of having the effect of providing benefits, in the form of pensions, allowances, and gratuities or otherwise, payable on termination of service, death or retirement, to or in respect of persons gainfully employed in Hong Kong or elsewhere under a contract of service. An exemption to the compliance requirements under ORSO may be granted if the scheme is registered with or approved by an offshore authority that performs functions similar to those of the Hong Kong Registrar, or fewer than 10% or 50 of the scheme members, whichever is lower, are Hong Kong permanent residents.

The Mandatory Provident Fund Schemes Ordinance (MPFSO) sets out the framework for the Mandatory Provident Fund system in Hong Kong. In keeping with Hong Kong’s policy of encouraging commercial markets, the legislation establishes a mandatory retirement system, which is largely run by the private sector. The fundamental requirement of the MPFSO is that every employer of the relevant employees must establish or join a Mandatory Provident Fund scheme. Non-Hong Kong employers will be subject to the legislation if they have employees in Hong Kong. A “relevant employee” is defined as an employee of between 18 and 65 years of age, including apprentices.

The MPFSO contains a number of specific exemptions, including ones for expatriate workers and members of existing schemes.

The employer is required to contribute 5% of the employee’s relevant income to a Mandatory Provident Fund scheme. Employees who are members of a Mandatory Provident Fund scheme are required to contribute 5% of relevant income up to a ceiling contribution level but may contribute in excess of the ceiling.

In Japan, there are three basic types of retirement plan:

the unfunded severance benefit plan

the corporate pension plan

the Employees’ Pension Fund

The unfunded severance benefit plan usually distributes a lump sum severance benefit when an employee terminates employment.

In recent years, Japanese law provides for two corporate pension systems: the Defined Benefit Pension Plan and the Corporate Type Defined Contribution Pension Plan, both of which incorporate greater employee protection than prior pension regimes.

The Employees’ Pension Fund is generally only available to employers with 500 or more employees and is a means for an employer to contract out of the earnings-related part of the social security pension program.

US Tax Consequences of Participating in Non-US Plans

Potential US federal income tax consequences is one of the most important considerations in determining whether an expatriate should participate in a non-US pension or other employee benefit plan.

If an employee participates in a non-US plan funded through a trust, the tax consequences are determined under Code Section 402(b), which generally provides that contributions must be included in the employee’s gross income when vested. Note that limited relief is provided under several US income tax treaties (e.g., Canada and UK).

An employee who participates in a non-US plan or a plan funded using a non-US trust should also address any potential issues under Code Section 409A and 457A. A non-US retirement plan is potentially subject to these rules because it provides a form of non-qualified deferred compensation.

A complete review of the Code Section 409A and 457A rules is beyond the scope of this discussion. Please see the discussion of Code Section 409A and 457A in the chapter entitled “Income Tax and Social Insurance.”

ERISA Implications

Due to the breadth of the definitions in the Employee Retirement Income Security Act of 1974, as amended (ERISA), a non-US retirement plan may inadvertently become subject to ERISA. In general, ERISA applies to an employee benefit plan established or maintained by any employer engaged in commerce or in any industry or activity affecting commerce.

Non-US retirement plans are not typically impacted by ERISA because ERISA exempts a plan maintained outside the US primarily for the benefit of persons, substantially all of whom are non-resident aliens. The US Department of Labor — which has primary jurisdiction for the interpretation and enforcement of ERISA — determines whether plans qualify for this exemption using factors such as:

whether the plans cover all or primarily all non-resident aliens

whether the work location of the employees is outside the US

whether the plan records and documents are maintained outside the United States

Whether a plan can meet this ERISA exemption is a fact and circumstances-based determination.

Equity Compensation

A number of local tax, securities, exchange control, data privacy and other issues arise if an employer intends to grant equity compensation to the expatriate while working abroad. These issues need to be carefully considered since a violation of these local laws, even with respect to one employee, carries significant monetary fines and other penalties.

The tax consequences in each jurisdiction vary and do not always match US tax consequences. For example, some non-US jurisdictions tax a stock option at the time the employee actually exercises the option (e.g., Hong Kong, Japan, Mexico, Singapore and the UK). Other jurisdictions tax employees at the time a stock option is granted (e.g., in Belgium if the employee accepts in writing within 60 days of grant). Other jurisdictions have taxed the grant of stock options on vesting (e.g., in Australia for options granted between 1 July 2009 and 30 June 2015 that were subject to a “real risk of forfeiture”).

In addition, some jurisdictions have local tax-qualified plans (e.g., France and the UK). If the equity award is granted to the expatriate under such a plan, they will enjoy favorable income tax treatment (usually, deferred tax or reduced taxation).

Tax consequences are further complicated if the employee is granted an equity award in one jurisdiction but vests or exercises that award in another jurisdiction. Tracking what tax liability is owed to which jurisdiction is challenging, especially with employees that worked in multiple jurisdictions during their expatriate assignment.

The issues arise from both understanding the employee’s tax liabilities as well as the reporting and withholding obligations that the equity plan sponsor and employer are responsible for. Each jurisdiction has different rules regarding the sourcing of such compensation and income tax treaties afford little relief. Accordingly, it is difficult to uniformly handle the tax issues associated with equity compensation awarded to globally mobile employees.

Although US issuers are generally not entitled to an income tax deduction for equity awards related to employees working for a local subsidiary, the local subsidiary may be able to obtain a local income tax deduction related to such amount. In many jurisdictions, the income tax deduction of the local subsidiary is based on the execution of a written reimbursement agreement between the US parent company granting the equity award and the local subsidiary prior to the grant. Some jurisdictions do not permit such a deduction for equity awards under any circumstances (e.g., the Netherlands).

Granting equity compensation to an employee may trigger local securities law compliance issues, such as a local securities authorities’ filing requirement or distributing a prospectus document to employees. For example, Australia is often requires an offer document and filing. In Japan, grants of options to 50 or more employees of an indirect or less than wholly owned subsidiary with an offering value equal to or greater than JPY 100 million requires an extensive filing and annual reporting obligation. Grants of equity compensation, especially stock purchase plans, in Europe may require compliance with the EU Prospectus Directive. However, compliance has become easier for US listed and other non-EU listed companies with the expansion of the Directive’s “employee share plan exemption” to non-EU listed companies.

In certain jurisdictions, exchange control rules still play a large role in determining the ability of a corporation to offer equity compensation to an employee. In some jurisdictions (e.g., China and Vietnam), governmental approval from the exchange control authorities is required in advance before an equity plan can be implemented.

Furthermore, granting an equity award to an employee may require compliance with local data privacy and labor rules. Certain jurisdictions have formal legislation prohibiting the transmission of employees’ personal information (e.g., name, age, seniority) across borders, even to an affiliated company. Some jurisdictions require the employee to consent to the transfer of such information while others require the employee’s formal approval or notification to a local governmental authority, and some require both. As of May 2018, all multinational companies granting equity awards in the EU must review data privacy requirements to ensure compliance with the new EU data privacy requirements (GDPR). Other countries have mirrored the changes implemented in the EU and have also enacted more robust data privacy requirements, which must be reviewed in connection with any grant of equity awards.

The value of the equity compensation offered to the employee may give rise to acquired rights issues in certain jurisdictions, making it difficult to terminate the benefit in the future without the employee’s consent. Furthermore, the value of the equity compensation may needed to calculate a terminated employee’s severance pay, — creating a more expensive termination for the employer.

Please see the “Global Equity Compensation” chapter for a comprehensive discussion of the equity-related issues facing US expatriates and foreign nationals working in the United States.

Continuing US Health Benefits

If the employer is providing US group health plan coverage an expatriate and their family while they are living in a non-US jurisdiction, the plan should be reviewed for any coverage gaps and problems arising from the foreign assignment. For example, US group health plans often do not cover employees and their dependents while they are working outside of the United States. If a plan does provide such coverage, it may require the employee to pay their health care expenses upfront and then submit a claim for reimbursement.

In addition, if a foreign doctor or hospital fails to meet certain qualifications, a US group health plan refuse to reimburse an employee for certain medical bills. However, amending the US group health plan to address these problems may not be possible in certain instances (e.g., if the plan is self-funded or third-party insurers are involved).

Before the employee leaves on their assignment, the employer should review the plan document and consult with its insurer, plan administrator or legal counsel to determine whether coverage can be extended. Furthermore, the employer should determine whether the requirements of the Patient Protection and Affordable Care Act (PPACA) will continue to apply to the expatriate while they are working on foreign assignment. Specifically, if the expatriate will be required to maintain “minimum essential coverage” while working abroad. There are currently legislative proposals to repeal PPACA and adopt new legislation, which may result in different requirements for expatriate coverage.

Many multinationals sponsors have standalone global health plans for their expatriates, specifically to avoid any coverage issues under US domestic health plans.

An employer should also consider the US income tax consequences of providing health benefits to the employee and their through the US group health plan. Generally, if the employee is not employed by a US employer, or a foreign branch or a member of the US employer’s controlled group, the US employer’s contributions to the plan and the amounts the employee and their dependents receive through the plan no longer qualifies for tax exemptions under the Code.

Additionally, the employee and their dependents may lose the ability to make pre-tax contributions under the cafeteria plan if the US group health plan is financed by a cafeteria plan and the employee is no longer employed by a US employer or a foreign branch or a member of the controlled group of the US employer.

If the employee becomes a resident of the foreign jurisdiction and is subject to local laws during their foreign assignment, the potential impact of the foreign laws should also be considered. For example, premiums paid on behalf of the employee or benefits provided though the US group health plan may be taxable to the employee or their dependents under the tax laws of the foreign jurisdiction. The premiums or benefits may also be subject to employment tax withholding and the premiums or benefits may be included in the calculation of severance indemnity payments that an employer must make for dismissing the employee.

There may also be a problem providing insurance coverage for someone residing in a non-US jurisdiction if the US insurance company is not registered to conduct business in that country and the employee is a participant in an insured plan in the US. Failure to comply with this local registration requirement may render insurance agreements unenforceable in that jurisdiction and may also trigger monetary sanctions against the host country employer.

Depending on the situation, the employer may want to arrange to replace or supplement the coverage provided by the US group health plan. This arrangement may include:

the purchase of a specially designed individual policy

the enrollment of the employee and their family in a specially designed group health plan for expatriates, which is the common approach for many multinationals

the enrollment of the employee and their family in an overseas emergency medical services and evacuation program

the enrollment of the employee and their family in a non-US nationalized or socialized health program

Specially designed individual or group insurance policies or plans may be useful in addressing coverage gaps and other practical problems that arise because of the foreign assignment. Overseas emergency medical services and evacuation contracts may also be useful when evacuation to the United States is necessary to receive a certain type or quality of health care and for referral to qualified foreign health care.

Note that if the employee is no longer covered by the US group health plan as a result of the assignment, they (or any “qualified beneficiary”) will no longer be eligible to elect for COBRA continuation coverage if there is an event that would otherwise trigger COBRA coverage, as the employee would no longer be a “covered employee.” In this regard, inquiring whether the employee’s transfer of employment to a non-US employer could constitute a “qualifying event” for purposes of COBRA group health plan continuation coverage.

Non-US Health Benefits

The employee’s participation in a non-US health benefit plan may raise a number of issues. Many non-US countries have extensive governmental health programs. While non-local, private health plans exist in some countries, they may be structured to only provide supplemental benefits on top of the benefits provided by the governmental program. Whether an employee can participate in the underlying governmental program may depend on how long they have been residing in the non-US country or the satisfaction of other conditions. Accordingly, many employees try to retain some health benefit coverage in the United States while they are overseas.

The employee may desire supplemental health benefits (if local law does not prohibit them) because of limited non-US governmental program benefits. For example, some governmental programs may:

only provide ward-level care (e.g., no semi-private or private hospital rooms)

require the use of certain governmental or governmentally approved facilities or providers

have long waiting periods for certain types of non-emergency care

provide a lower quality care outside of major cities

not cover certain benefits (e.g., dental coverage)

not be used by employees due to a local class bias

may not cover all or part of the costs of health care received while the covered individual is temporarily out of the foreign country (e.g., in the United States on home leave or in another foreign country on a temporary work assignment)

Income Tax and Social Insurance



An employee who works abroad is always concerned about the possibility of increased income taxation and social taxation resulting from a foreign assignment. For example, will the employee be taxable in both the home country and the host country, resulting in double taxation of the employee’s compensation? Whether such increased taxation is likely, and whether it can be avoided, depends on a number of factors, such as the length of time the employee will be working in the foreign jurisdiction, the type of work the employee will do while working abroad, the employee’s citizenship, nationality or residency, and other similar factors. This determination will also need to take into account:

The income tax, social insurance and other relevant laws of the home and host jurisdictions

Special rules, if any, governing the cross-border transfer of employees in the home and host jurisdictions

The provisions of an income tax treaty, social security totalization agreement or other international agreement between the home and host jurisdictions

The employer will be equally concerned with the issue of increased taxation, since many expatriates are covered by a tax reimbursement policy whereby the employer will be responsible for paying the employee’s taxes which are greater than the employee’s “home country” tax liability. For further details, see “Tax Equalization and Tax Protection Programs” below.

The employer will also be concerned with avoiding a permanent establishment (PE) issue resulting from the activities of the employee working abroad — as the employer would be taxable in the host jurisdiction for the activities of the employee working there. For further details, see “Permanent Establishment Risk” below. In addition, the employer will also be interested in the availability of a corporate income tax deduction for the employee’s compensation and assignment-related costs. Finally, to the extent the employee is taxable by the host jurisdiction, the employer will want to confirm that the applicable withholding and reporting rules are followed, both in the home and host jurisdictions. For further details, see “Compliance: Withholding and Reporting” below.

As an example of how jurisdictions often approach these issues, this chapter focuses on some of the key US federal income tax and social security provisions that apply to expatriates, whether outbound or inbound. Space does not permit a discussion of all jurisdictions and their income tax and social tax rules, so it is recommended to consult with international tax counsel to understand the rules for any other jurisdictions. It is also recommended to work closely with tax counsel to understand the potential application of these or similar provisions to the facts of any particular assignment.

US Federal Income Tax: Short-term Assignments

Where an employee lives and works abroad, it is natural to assume that the country where they are assigned will seek to tax their compensation. Notwithstanding, many jurisdictions have provided income tax relief for short-term assignments. Understanding how these rules work in a particular country is key to effective tax planning.

If there is no relief under the host country’s domestic tax law for employees who are short-term business visitors in that jurisdiction, often there may be relief under an applicable income tax treaty entered into between the host jurisdiction and the home jurisdiction.

As of the date of publication, the United States has income tax treaties in force with more than 67 countries. Several income tax treaty provisions may be relevant to mobile employees such as provisions addressing “dependent personal services” or “income from employment,” as these provisions are primarily directed at employees who are sent to work on short-term assignments in the host jurisdiction by their employers.

For example, Article 14 of the US-UK Income Tax Treaty provides a general rule and two exceptions regarding income from employment. The general rule is that salaries, wages and other similar remuneration derived by a resident of the home country in respect of employment is only taxable in that country, unless the employment takes place in the host country. If the employment takes place in the host country, the host country may tax it.

However, remuneration derived by a resident of the home country with respect to employment in the host country will only be taxable in the home country if:

The individual is present in the host country for a period or periods not exceeding 183 days in any 12-month period commencing or ending in the taxable year

The remuneration is paid by or on behalf of an employer who is not a resident of the host country

The remuneration is not borne by a permanent establishment that the employer has in the host country

Therefore, if an employee is treated as a US resident under this treaty, the employee may avoid UK income tax on remuneration resulting from employment in the UK if: (i) they are not present in the UK for more than 183 days during any 12-month period (ii) they are paid by or on behalf of an employer outside of the UK and (iii) the remuneration is not deducted by a permanent establishment that the employer has in the UK.

Many US tax treaties have similar, but not always identical, language. Some treaties look at whether the employee has spent more than 183 days in a calendar year in the host country (in addition to the other requirements). In other cases, the time limit may be less than 183 days or there may be a maximum compensation limit imposed.  
It should be noted that the Organization of Economic Community and Development (OECD) has indicated that the “employer,” for the purposes of treaty analysis, is not necessarily the legal employer. The OECD recommends that the “economic employer” concept be used in applying this type of income tax treaty provision. An “economic employer” is deemed to be the one who actually directs and controls the activities of the individual. The “legal employer” is the one who is denominated as the employer on paper.

Consequently, when structuring short-term assignments in countries that have adopted the “economic employer” concept, the activities and actions of the employee need to be reviewed. The treaty exemption will only apply if the home country entity meets the “economic employer” test and if other tests are met (i.e., 183 days and no chargeback of compensation costs to the host entity).

In a similar fashion, if the employee intends to rely on this treaty exemption, compensation costs related to the employee should not be charged against and reimbursed by a host country entity or permanent establishment in the host country. Note that in some cases the existence of a treaty exemption, such as this one, may not necessarily exempt the employee from making an individual income tax filing in the host country.

Treaty provisions providing relief from the potential double taxation of retirement plan participation or pension plan distributions, or with respect to stock option-related income, may also be available depending on which treaty is involved. These provisions should be reviewed and considered, especially in cases of longer-term assignments. However, these provisions are currently only present in a small number of US income tax treaties.

Traveling and Temporary Living Expenses

Under US income tax rules, an employee may be able to exclude traveling and temporary living expenses while “away from home” in the pursuit of a trade or business (including amounts expended for meals and lodging that are not lavish) from gross income amounts paid by the employer. Internal Revenue Code (Code) Section 162(a)(2) allows an exemption for living expenses that are ordinary and necessary while the employee is temporarily away from home.

Whether an employee is “away from home” is a facts and circumstance based determination. However, in no event can an international assignment be considered “temporary” if it is expected to, or does, last for more than one year.

US Federal Income Tax: Long-term Assignments

In addition to the income tax relief the United States provides to its taxpayers who are on short-term assignments, it also provides some relief for US taxpayers who are on long-term assignments (which last one year or more).

Foreign-Earned Income and Housing Exclusion

One of the most valuable tax planning devices for a US employee who is working outside of the United States is the ability to elect to exclude “foreign earned income” and a “housing cost amount” from gross income under Code Section 911.

The maximum amount of foreign-earned income that can be excluded is indexed and is USD 108,700 for 2021. It can be only elected by a “qualified individual,” meaning a person whose “tax home” is in a foreign country and who is either:

A US citizen who is a bona fide resident of a foreign country for an entire taxable year; or

A US citizen or resident who is present in a foreign country or countries for at least 330 full days of such period during any period of 12 consecutive months

A qualified individual must elect to exclude foreign-earned income on IRS Form 2555, or a comparable form, which must be filed with the individual’s US federal income tax return for the first taxable year for which the election is to be effective. Individuals who expect to be eligible for the exclusion may adjust their federal income tax withholding by completing an IRS Form 673 and filing it with their payroll department.

In addition to the foreign-earned income exclusion, a qualified individual may elect to exclude a “housing cost amount” from gross income, which relates to certain housing expenses attributable to “employer-provided amounts.”

The term “employer-provided amounts” means any amount paid or incurred on behalf of the individual by the individual’s employer that is foreign-earned income for the taxable year without regard to Code Section 911. Thus, salary payments, reimbursement for housing expenses or amounts paid to a third party are included. Furthermore, an individual will only have earnings that are not “employer-provided amounts” if the individual has earnings from self-employment.

If the individual’s qualified housing expenses exceed USD 17,392 (for 2021) (i.e., 16% of the maximum foreign-earned income exclusion for a full taxable year), the individual may elect to exclude the excess up to a maximum of USD 32,610 (for 2021) (i.e., 30% of the maximum foreign-earned income exclusion for a full taxable year). However, the IRS has issued guidance providing upward adjustments to this maximum in a number of high housing cost locations.

A qualified individual may make a separate election to exclude the housing cost amount on the same form and in the same manner as the foreign-earned income exclusion. An individual does not have to make a special election to claim the housing cost amount deduction.

However, the individual must provide the following information:

Name

Address

Social security number

Name of employer

Foreign country where tax home is established

Tax status

Qualifying period of bona fide residence or presence

Foreign-earned income for the taxable year

Housing expenses

Foreign Tax Credit

Another valuable tax planning device for a US employee who works outside of the United States is the ability to receive a tax credit for foreign or US possession income tax paid or accrued during the taxable year. The credit also applies against taxes paid in lieu of income taxes (a category that includes withholding taxes).

Note that an individual may not take a credit for taxes paid on foreign income that is excluded from gross income under Code Section 911. The credit is available to any employee who is a US citizen, resident alien of the United States or a resident alien who is a bona fide resident of Puerto Rico for the entire taxable year.

The foreign tax credit is subject to a specific limitation. It is generally limited to the same proportion of the employee’s total US tax that the employee’s foreign-source taxable income — but not in excess of the entire taxable income — bears to the entire taxable income for the taxable year.

Whether an employee has foreign-source taxable income for the purposes of this limitation depends on the type of income involved and, in some cases, the residency status of the employee.

For example, with respect to wages, the employee has foreign-source income if the services are performed in a foreign country. With respect to interest, the employee has foreign-source income if the interest is credited to a bank account in a foreign country or if the employee invests in foreign bonds that pay interest in a foreign currency. Income from the sale of personal property by a US resident is US-source income regardless of the place of sale. Similarly, income from the sale of personal property by a non-resident is generally sourced outside the United States.

In the event that an employee cannot use all of the foreign tax credit, they are permitted to carry the unused credit back for one year and to carry forward the unused credit for 10 years. This means that the employee can treat the unused foreign tax of a tax year as though the tax were paid or accrued in the employee’s first preceding and 10 succeeding tax years up to the amount of any excess limitation in those years.

Participation in Non-US Compensation Programs

Where an employee on foreign assignment becomes a participant in a compensation or benefit plan sponsored by an employer in the host country, such participation may have US income tax consequences — especially in connection with the rules under Code Section 409A and 457A regarding deferred compensation.

A complete review of Code Section 409A and 457A rules is beyond the scope of this discussion. In general, if a person has a legally binding right in one taxable year to receive an amount (either as compensation or as reimbursement or otherwise) that will be paid in a subsequent taxable year, that amount is considered deferred compensation for the purposes of Code Section 409A unless it meets one of the exemptions.

Assuming that no exemption to Section 409A applies, amounts that are considered deferred compensation must comply with various requirements regarding the time and form of the payment, timing of deferral elections and a six-month delay of separation payments made to certain “key employees” of a public company to mitigate adverse income tax consequences. In addition, there are prohibitions under Section 409A on offshore funding and funding tied to the employer’s financial condition. If the requirements are not met, the deferred compensation amounts will be taxable to the employee at the time of vesting and an additional 20% tax will be imposed.

Since Code Section 409A rules apply to all plans globally that have US taxpayer participants, the issue should be carefully considered for any non-US compensation plans (e.g., retirement plans, equity incentive plans and cash bonus plans) in which the expatriate will participate. It is highly unlikely that such plans will be designed to avoid or comply with the Code Section 409A requirements.

As a first step of the analysis, it is critical to identify all of the potential compensation plans that will be offered to the employee, including, for example, equity compensation plans. The Code Section 409A rules do provide a few specific exemptions for foreign plans, although they are limited in scope.

For example, a foreign retirement plan may qualify for an exemption from Code Section 409A as a “broad-based retirement plan.” US citizens and green card holders will be able to qualify for this exemption if:

They are not eligible to participate in a US-qualified plan

The deferral is non-elective and relates to foreign-earned income

The accrual does not exceed the amount permitted under Code Section 415 (i.e., the US-qualified plan limits)

The broad-based plan must also meet the following requirements:

The foreign plan must be in writing.

The foreign plan must be non-discriminatory in terms of coverage and amount of benefit (either alone or in combination with other comparable plans).

The foreign plan must provide significant benefits for a substantial majority of the covered employees and contain provisions, or be subject to tax law provisions or other restrictions, which generally discourage employees from using plan benefits for purposes other than retirement and restrict access to plan benefits before separation from service.

There are also Code Section 409A exemptions for plans exempt under a tax treaty, foreign social security plans and plans that are considered funded by a trust under the rules, among others.

In addition, Code Section 457A can also apply to deferred compensation earned by US taxpayer employees working abroad. It limits the ability to offer deferred compensation in cases where employees (who are subject to US taxation) perform services for employers who are considered “non-qualified entities.” In general, employers based in jurisdictions that do not have a corporate income tax will be “non-qualified entities.”

Furthermore, an employer based in a jurisdiction that has a corporate income tax and an income tax treaty with the United States may be considered a “non-qualified entity” (depending on the extent to which the jurisdiction taxes non-resident income differently from resident income and the extent to which the employer’s income for the year includes non-resident income). Given the complexities of Code Section 457A, employers are encouraged to consult with tax counsel regarding the potential impact of this section on their expatriate population.

US Federal Income Tax — US Inbound Assignments

Employees who are sent to work in other countries, even for relatively short assignments, may nonetheless be subject to local income tax on the compensation they earn for working abroad unless there is a local tax exemption for such limited work or an income tax treaty provision provides an exemption. In the United States, for example, the Code provides a limited exemption for foreign employees working in the United States on a short-term basis, but it is practically of no use since the compensation earned during the period of assignment cannot exceed USD 3,000. Other jurisdictions may have similar statutory exemptions for short-term assignments but, generally speaking, they are rare.

Taxation as a “Resident”

The principal concern for an employee who comes to work in the United States (and who is not a US citizen or does not want to become a US citizen) is whether they will be taxed as a resident alien or a non-resident alien.

As a resident alien, they will be taxed in the same manner as a US citizen, namely, all worldwide income, including any compensation paid or earned outside of the United States, will be subject to US federal income tax. A resident alien is permitted to offset this US tax liability by a tax credit or a tax deduction for foreign income taxes paid on compensation income, if any, subject to certain limitations.

As a non-resident alien, they will only be taxed on income “effectively connected” with the conduct of a US trade or business at the same rate and in the same manner as US citizens and residents, but with some limitations (e.g., generally not able to file a return jointly with a spouse). In addition, absent a tax treaty exemption or reduced rate of tax, there will be a flat 30% tax rate on certain investments and other fixed or determinable annual or periodic income from sources within the United States that is not “effectively connected” with the conduct of a US trade or business.

The employee’s performance of services in the United States will be deemed to be the conduct of a US trade or business. Therefore, the compensation received will be “effectively connected” with a US trade or business and taxable at the same rate as that for US citizens and residents.

In general, an employee will be treated as a “resident alien” for tax purposes if the employee:

Is lawfully permitted to reside permanently in the United States (i.e., the “green card” test)

Is in the United States for a substantial amount of time (i.e., the “substantial presence” test)

The “green card” test is as its name suggests. This covers foreign nationals granted alien registration cards called “green cards” (even though the cards are not green).

The “substantial presence” test is satisfied if, in general:

The employee is present in the United States for at least 31 days during the current calendar year.

The sum of the days they are present in the United States during the current calendar year, plus one-third of the days they were present in the preceding year, and one-sixth of the days they were present in the second preceding year, is equal to or exceeds 183 days.

There is an exception to the “substantial presence” test if a foreign national is present in the United States for fewer than 183 days during the year and has a tax home in, and closer connection to, a foreign country.

If the employee does not satisfy either of the two tests described above, it is possible to elect to be treated as a resident under certain circumstances.

A non-resident alien who is temporarily present in the United States as a non-immigrant under the foreign student F visa or exchange visitor J visa, may exclude from gross income compensation received from a foreign employer or an office maintained outside of the United States by a US person.

In addition, wages, fees or the salary of an employee of a foreign government or an international organization are not included in gross income for US tax purposes if:

The employee is a non-resident alien or a citizen of the Philippines

The services as an employee of a foreign government are similar to those performed by employees of the US government in foreign countries

The foreign government grants an equivalent exemption to US government employees performing services in that country

Finally, non-resident aliens may be entitled to reduced rates of, or exemption from, US federal income taxation under an applicable income tax treaty between the country of which they are residents and the United States.

A non-resident alien who claims an exemption from US federal income tax under a provision of the Code or an applicable treaty must file a statement with the employer giving their name, address, taxpayer identification number, and the reason for exemption certifying that the individual is not a citizen or resident of the United States and the compensation to be paid during the tax year is, or will be, exempt from income tax. If exemption from tax is claimed under a treaty, the statement must also indicate the under which provision and treaty the exemption is claimed, the country of which the non-resident alien is a resident and sufficient facts to justify the claim for exemption.

Participation in Non-US Compensation Programs

As previously discussed, Code Section 409A has a very broad application. In the case of employees who come to work in the United States, there is also a concern that certain non-US plan benefits they receive while working in the US could be subject to the adverse consequences of Code Section 409A. Accordingly, the employee’s participation in non-US compensation programs must be reviewed for Section 409A compliance, the same as for US programs.

For example, some non-US stock option plans may not meet the requirements of the fair market value grant exemption from Code Section 409A. Stock option plans that provide for an exercise price that is less than the fair market value on the date of grant may have this problem. If a foreign national was granted stock options outside of the United States, arrives to work in the United States and becomes a “resident alien” of the United States, then unexercised stock option grants under such plans may be particularly problematic under Code Section 409A.

Notwithstanding, there are some exemptions under Code Section 409A for deferred compensation that vests before the employee becomes a US tax resident. Again, as in the case of all US employees who go to work abroad, it is critical to identify all of the plans and arrangements that could potentially be subject to taxation under Code Section 409A in advance of an employee’s assignment to the United States.

US Social Security

One of the major concerns for an employee working outside of his home jurisdiction is whether compensation will be subject to local social insurance taxes (Social Security) in the United States. The concern arises from the employer’s standpoint as well, as in many jurisdictions social insurance taxes on compensation are imposed on the employer as well.

Social Security taxes in the United States (commonly referred to as “FICA” taxes) are relatively low in comparison with those of other jurisdictions. Therefore, it is a common desire to remain covered by US Social Security and avoid the imposition of local social insurance taxes wherever possible for a US employee who is working abroad. Continuing to be covered by US Social Security also allows the employee to build up his eligibility for a maximum Social Security benefit upon retirement.

In general, Social Security contributions must be paid on the earnings of a US citizen or resident alien working for an American employer anywhere in the world. An “American Employer” is defined as:

The United States or any instrumentality thereof

An individual who is a resident of the United States

A partnership, if two-thirds or more of the partners are residents of the United States

A trust, if all of the trustees are residents of the United States

A corporation organized under the laws of the United States or any state

Special rules apply to companies that contract with the US federal government so that certain foreign entities may also be considered American Employers for the purposes of this rule.

Thus, a US employee who is seconded to work abroad and continues to be employed by an American Employer will remain covered by US Social Security and FICA taxes will be withheld from their compensation as a result.

Similarly, a US employee who works outside the United States for a foreign branch or division of an American Employer will remain covered by US Social Security as a branch or division is technically a mere extension of the home company.

On the other hand, a US citizen or resident who is employed outside of the United States by an employer who is not an American Employer will not remain covered by the US Social Security system and, therefore, FICA taxes will not be required to be withheld from his compensation.

Notwithstanding, there is a special election available for certain employees to remain covered by US Social Security while working abroad. If a US citizen or resident is working for an American Employer and if the US employee is sent by that American employer to work for a “foreign affiliate,” as defined below, then the American employer may enter into a voluntary agreement under Section 3121(l) of the Code to continue the US Social Security coverage of that individual. A “foreign affiliate” is defined as a foreign entity in which an American employer owns at least a 10% interest. This voluntary, but irrevocable, agreement extends US Social Security coverage to services performed outside of the United States by all employees who are citizens or residents of the United States.

Under this voluntary agreement, the American employer pays the employer’s and employee’s portion of FICA taxes that would be imposed if such wages were subject to FICA taxes under the general rules. There is no legal requirement for the employee to reimburse the American employer for the employee’s share of the tax, although some companies do in fact require such reimbursement.

Totalization Agreements

Just as the expatriate and their employer might want to avoid the problem of increased income taxation resulting from the foreign assignment, there is also a desire to avoid the problem of double social taxation.

Double social taxation occurs when an employee remains covered by the social insurance taxes of their home jurisdiction and becomes covered by the social insurance taxes of the host jurisdiction. For example, a US employee who is seconded to work abroad (and therefore remains employed by an American Employer), will remain covered by the US Social Security system. At the same time, the host jurisdiction may impose its social insurance taxes on the employee’s compensation merely because the employee works there (a fairly common standard in non-US jurisdictions). In such a case, contributions to both social tax systems may be required on behalf of the employee and also by the employer — reducing the employee’s compensation and increasing both the employee’s and employer’s social tax burden.

The employee may also encounter fragmented social security coverage. A US citizen (or resident) who has worked for less than 10 years and transfers employment to a foreign employer (that is not an American Employer) will not continue to earn “quarters of coverage” for a maximum US Social Security benefit. In addition, if the expatriate’s employment history includes a lot of temporary assignments in different foreign jurisdictions, the employee may find that they have not worked long enough in any one jurisdiction to qualify for an old age, retirement or other social benefit under any system of the country at the end of their career.

To address these problems, many jurisdictions have entered into international agreements called totalization agreements. These international agreements provide a set of rules to determine which jurisdiction will cover the individual’s employment under its social insurance tax system (Totalization Agreements). Note that a Totalization Agreement does not change the domestic rules of a country’s social tax system and does not impose social insurance tax coverage if employment would not ordinarily be covered.

In the United States there are 30 Totalization Agreements in force. In general, each Totalization Agreement follows the “territoriality” principle where employment for purposes of social insurance taxes is covered only by the laws of the country in which the work is performed.

An exception to this territoriality rule exists where the employee is sent by the home country employer to be on temporary assignment in the other jurisdiction. In that case, the employee will remain covered by the social insurance system of the home country. An assignment is temporary if it last five years or less. Note that there are some variations to these rules, so it is recommended to check the applicable Totalization Agreement to determine which provisions apply in each case.

With regard to benefits, a Totalization Agreement permits an employee to combine (or totalize) periods of coverage for the purposes of determining eligibility for coverage. For example, to qualify for a minimum US Social Security benefit under the totalization procedure, the executive must have at least six quarters of coverage in the United States system. The Totalization Agreements contain parallel provisions for each country, so that if the combined (or totalized) periods of coverage are sufficient to meet the eligibility requirements for benefits, then pro rata benefits are payable from each country’s social insurance system.

An employee must obtain a certificate of coverage from the responsible authorities in their home jurisdiction to verify continued coverage while working abroad in order to take advantage of the “temporary assignment” exemption.

In the United States, an application for such a certificate must be made by the employer to the Social Security Administration (SSA), and must contain the following information:

Full name of the outbound mobile employee

Date and place of birth

Citizenship, country of permanent residency

Social security number

Date and place of hire

Name and address of employer in the United States and the other country

Dates of transfer and anticipated return

If the employee is transferring to France, the employee must also certify that there is medical coverage under a private insurance plan, as France imposes this certification requirement on anyone who seeks exemption from French social security tax. In many cases, the certificate of coverage can be obtained from the SSA by applying online.

Social Security Implications for Inbound Assignments

In the case of an employee assigned to work in the United States by a foreign employer, such employment will be subject to US Social Security coverage (e.g., FICA taxes) unless the performance of services does not come under the definition of “employment” for US Social Security purposes. For example, there is a specific exemption for non-resident aliens who are present in the United States under the F or J visa.

An inbound employee who does not qualify for those exemptions from US Social Security will be subject to FICA tax withholding on compensation, unless an exemption under a Totalization Agreement in effect with the home country can be claimed. For example, if the employee is on a temporary assignment, then the applicable Totalization Agreement can be relied upon as an exemption from the application of FICA tax withholding. In that event, the employee will need to produce a certificate of coverage from the home country authority to claim the exemption.

Employee Reporting Obligations

Employees who are US tax residents should also be aware of the individual reporting requirements under the Foreign Account Tax Compliance Act (FATCA) and in connection with the Foreign Bank and Financial Account requirements. Specifically, “foreign financial assets” is defined rather broadly in the FATCA. Foreign financial assets can include shares of foreign companies, balances under foreign compensation plans and other arrangements sponsored by foreign affiliates. Certain taxpayers may also have to complete a Form 8938 (Statement of Foreign Financial Assets) and attach it to their annual US income tax return. Given the complexities of these reporting obligations, employers are encouraged to consult with tax counsel regarding the potential impact of these requirements on their expatriate population because there are significant penalties for failing to report on time.

Selected Concerns from the Employer’s Perspective

**Availability of Corporate Income Tax Deduction**

One of the primary issues from the employer’s standpoint is whether the costs of the expatriate’s compensation are deductible, and if so, by which entity. Under US federal income tax principles, the entity that is the common law employer, (the entity that has the right to direct and control the activities of the employee) is entitled to the income tax deduction. This principle may be similar in non-US jurisdictions, so it would be prudent to consult with a tax adviser on any tax deduction question.

Under US tax principles, if the employee is seconded to work abroad for another company, they remain a common law employee of the sending employer and that employer is entitled to deduct the costs of the employee’s compensation.

Similarly, if the employee’s employment is transferred to another company (another corporate entity, such as a subsidiary, a parent company or a brother-sister company), it is that other entity that has the right to deduct the costs of the employee’s compensation. Even if the company is in the same corporate group as the employee’s former employer, the former employer is not entitled to deduct the costs of compensation because the benefit to such employer is deemed to be only an indirect or derivative benefit. For these purposes, a division or branch is deemed to be the same as the corporate entity to which it relates, and is not considered a separate entity for income tax deduction purposes.

**Permanent Establishment Risk**

One key issue that always needs to be considered in structuring international assignments is whether the employment structure will inadvertently create a permanent establishment (PE) issue for the home country employer. A PE exists where the employing entity is considered to be doing business in the host country and is therefore subject to corporate income tax by the host country on an allocable amount of the entity’s net income. As discussed in the chapter on Employment, an employee remains employed by, and therefore directed and controlled by, the home country employer in a secondment structure. Accordingly, this structure creates a PE risk for the home country employer. The length of the assignment does not necessarily matter — risks still arise when an employee is on a short-term or “informal” assignment (where the employee is seconded to work in another jurisdiction for just a few weeks or months).

A company that creates a PE is often obligated to file tax returns with a foreign tax agency, to observe local accounting standards for foreign tax purposes and to pay higher taxes on a worldwide basis. The existence of a PE may also trigger registration, filing and publication obligations for the company that would not otherwise exist.

A local tax inspector may assume that a company has automatically created a PE if the expatriate is on secondment while working in the host jurisdiction. To mitigate this risk, many multinational companies include express language in the expatriate’s assignment letter specifying that the expatriate has no authority to conclude contracts on behalf of the home country employer while working in the host jurisdiction. However, this protective language does not always work. Consultation with international tax counsel is recommended.

Activities that could constitute a PE vary by jurisdiction and are based on income tax treaty provisions as well as the structure of the employment relationships. The concept of PE has undergone significant changes since OECD issued guidance. As a result of these changes, a covenant expressing that the expatriate does not have the authority to conclude contracts may not be enough to avoid a PE risk in some jurisdictions. In some jurisdictions (e.g., China), secondment attracts special scrutiny, both because it is a secondment and it creates a potential tax liability for the home country employer (unless the expatriate is directed and controlled by the local entity in China). In other jurisdictions (e.g., India and Canada), the secondment structure may run afoul of the Services PE concept — a PE may exist merely because an employee of the home jurisdiction performs services in the host jurisdiction. We recommend that companies work closely with their tax advisers to understand the nuances and potential exposures that may arise in connection with the PE risk.

**Tax Equalization and Tax Protection Programs**

To minimize the expatriate’s potential exposure to a higher global income and social security tax burden, the employer will often implement a tax equalization or tax protection program for all of its expatriates and globally mobile employees. Such a program provides a consistent approach for handling the complex income and social security tax situation of any particular expatriate.

A tax equalization program provides that the employee’s tax burden on equalized income will be neither greater nor less than the income and social taxes (the “stay-at-home tax” or “final hypothetical tax”) they would have paid had they not gone on a foreign assignment. It requires the employee to pay a retained hypothetical tax approximating the stay-at-home taxes. In a typical tax equalization program, the hypothetical tax is computed at the beginning of the year and a pro rata amount is deducted from the employee’s wages each payroll period. At the end of the year, the employee’s hypothetical income and social taxes are recalculated based on the employee’s actual equalized income for the year. A reconciliation is then prepared to compare the employee’s final hypothetical tax liability with the employee’s hypothetical tax deducted during the year to determine whether the correct amount was withheld. If the amount of the hypothetical tax deducted during the year is greater than the final hypothetical tax liability, the difference is reimbursed to the employee. If the result is that too little hypothetical tax was deducted during the year, the employee must pay the difference to the company. The objective of the tax equalization program is to eliminate the tax windfall that an employee who moves from a high-tax jurisdiction to a low-tax jurisdiction could enjoy by virtue of lower tax rates.

A tax protection program also involves the calculation of a hypothetical tax. However, it is intended to only reimburse the employee in the event the employee incurs additional tax liability as a result of the foreign assignment (e.g., where the employee ends up working in a higher taxing jurisdiction).

Therefore, under a tax protection program, an employee is reimbursed the difference if the actual home and host country income and social taxes are more than the hypothetical tax deducted during the year .If the actual taxes are less than the hypothetical tax liability, the employee is not required to pay anything back to his employer and would benefit.

There are many variations on tax equalization and tax protection programs. Some employers cover state, local, US federal, foreign income and social taxes. What type of income is included, and excluded, depends on the company and the discussions it has with its tax advisers.

Since tax equalization and tax protection programs represent payments of compensation over a number of tax years, for US taxpayer employees there are potential Code Section 409A issues. The company providing such a program needs to ensure that the tax equalization/tax protection program complies with Code Section 409A. Consultation with tax counsel is often needed for this purpose.

As a best practice, the international assignment policy should be changed to comply with, or be exempt from, Code Section 409A.

Given the complexity of the hypothetical tax calculation, some companies will engage the services of an accounting firm to make the necessary determinations and prepare the various income tax returns for each affected employee. Employers do this both to be confident that its employees are handled consistently and that their tax returns are timely prepared and filed.

**Budgeting and Cost Projections**

Given the significant incremental costs generally related to an international assignment (e.g., employer-paid housing, additional allowances, tax reimbursements, home leaves, transition allowances), the company should prepare cost projections of, and accrue, for the total expected international assignment cost (including estimates of home and host country income and social tax), in cases where the employee is eligible for either tax equalization or tax protection.

**Compliance: Withholding and Reporting**

Global mobility has received more attention recently given that multinational companies have been focusing more on compliance-related issues. Specifically, companies often review their processes and procedures to confirm that: (i) all expatriates, extended business travelers and rotators are accounted for, (ii) the appropriate taxes (income, social taxes) are withheld from their employees’ pay and (iii) that the appropriate reporting of such pay is being conducted. More often than not, withholding and reporting problems occur when compensation is paid outside of the jurisdiction where the employee is working or there is a lack of clarity or a lack of direction to the payroll department regarding which entity is obligated to withhold on compensation and at what applicable rate. Details regarding individual participants who are working in, perhaps, dozens of jurisdictions sometimes become complex and burdensome to monitor when a large number of expatriates are on assignment or working remotely.

Notwithstanding these challenges, vigilance is paramount. Local tax authorities, based on recent audits and news accounts, have announced their intention to focus more on the activities of expatriates and their employers to ensure compliance with applicable tax withholding and reporting obligations is maintained. As local governments search for more revenue to address their fiscal budget concerns, they will look harder at this area.

Global Equity Compensation



Equity compensation awards held by employees present new issues when those employees become globally mobile.

As multinational employers increasingly seek to motivate and retain qualified executives and employees by offering equity-based compensation and, at the same time, transfer such individuals across international borders on short- or long-term assignments, it is important to identify and address the tax, social security and legal impact of such international transfers on equity compensation arrangements. Due to the complexity and global reach of US federal tax and social security regulations, the transfer of employees into and out of the US poses particular challenges that need to be considered in advance of any such transfer of employment.

Key Government Agencies

The Internal Revenue Service and Social Security Administration are the government agencies responsible for overseeing the assessment and payment of federal income taxes and social security taxes (i.e., Federal Insurance Contribution Act taxes, such as social security and Medicare tax).

In addition, the taxation of mobile employees is significantly impacted by tax treaties and other international agreements and acts, published by the US Department of State, and by social security Totalization Agreements negotiated and signed by the Department of Health and Human Services under the US Social Security Act. For American Employers, which includes corporations organized under the laws of the United States or any state, by sending employees to work in a Totalization Agreement country for five years or less, the SSA has oversight over the issuance of Certificates of US Social Security Coverage. This may enable such employees to remain subject to the US social security system and be exempt from social security taxes in the country to which they have been transferred.

Depending on the time an equity award holder spends in a particular state and municipality, state and local income tax and payroll tax authorities also have a stake in the taxation of equity awards held by mobile employees.

Finally, the Securities and Exchange Commission and the state securities regulators have oversight over any offerings of equity awards to employees in the US and the resale of shares acquired by those employees. In some instances, exemptions are available to the issuer as the offering is to employees, however, securities laws should be considered each time an equity award is granted or exercised or shares are resold.

Current Trends

There has been an increasing awareness among US and other global tax authorities that significant amounts of taxes may be owed on income that is derived from stock options and other forms of equity compensation awards held by employees who transfer employment across international borders. The focus arises from a commentary first published by the Organization for Economic Co-operation and Development in 2002, which addressed the tax difficulties of stock options in a cross-border context.

Further, in December 2008, the IRS announced that it added foreign withholding tax compliance to its list of issues with the highest “Tier I” organizational priority and coordination. Since then, there has been significant audit activity in this area. Although the IRS’s immediate focus was on the withholding of taxes on income paid to non-US resident individuals under Section 1441 of the Internal Revenue Code, its increased scrutiny of cross-border withholding practices conveys that companies granting equity awards to US-inbound and outbound globally mobile employees cannot afford to ignore proper US tax compliance. In 2014, the IRS amended the rules for withholding on US-source income received by foreign persons and in August 2015, an audit guide for equity (stock)-based compensation was published. The audit guide does not provide any specific guidance on globally mobile employees, but given its interest in equity-based compensation and its prior statements regarding foreign withholding tax compliance, it is expected that the IRS will inquire about globally mobile employees as part of any audits it conducts related to equity compensation. Historically, while employers and tax authorities have generally had arrangements in place to determine and assess the US and foreign taxes owed on salary paid to internationally mobile employees, the proper taxation of income from equity compensation awards has sometimes been overlooked. Consideration has not always been given to the fact that equity award income has usually been earned over a period of one or more years, during which the equity award holder may have been employed and resided in a number of different countries, each of which may assert taxable jurisdiction over the award.

However, at present, both US and foreign tax authorities are aware of the potential trailing tax liabilities relating to income from equity compensation arrangements, and are increasing their attention on this area. It is therefore important for multinational companies that have granted equity compensation awards to globally mobile employees, to identify the tax and social security issues affecting the taxability of income from such awards and to develop strategies for dealing with these issues while tracking international tax liabilities upfront.

Business Travel

Depending on the circumstances, non-US resident employees coming to the United States on short-term business trips (e.g., total stay of up to six months) may be subject to US federal income taxation on their wages paid during such business trips. This is based on the general US sourcing rule in Section 861 of the Internal Revenue Code that compensation for labor or personal services performed in the US is US-source income and therefore subject to US income tax unless an exemption applies. Where an individual (e.g., a business traveler) performs services partly in and partly outside the US, the applicable US Treasury Regulations provides that the portion of the individual’s compensation for such services that constitutes US-source income should, in many cases, be apportioned on a time basis.

In terms of equity awards, Treasury Regulations Section 1.861- 4(b)(2)(ii)(F) characterizes income from stock options as “multi-year compensation,” (i.e., compensation that is included in the income of an individual in one taxable year, but that is attributable to a period that includes two or more taxable years). Where stock options are held by an employee who spends time employed both inside and outside the US, the regulations indicate that it will generally be appropriate to measure US-source income by reference to the number of days the employee worked in the US, between the option grant date and the date on which all employment-related conditions for the exercise of the option have been satisfied (i.e., the vesting date, relative to the total days worked during the vesting period. This rule is modified in a small number of cases by a tax treaty between the US and the country in which the employee is resident). This concept applies equally to other forms of equity award such as restricted stock units which vest over a vesting period and employee stock purchase plan rights which vest/become exercisable over a purchase period.

As a result, if US federal income tax applies to wages paid to a foreign national business traveler during a US business trip, it will also apply to any income the individual receives from an equity award that is attributable to the US under the above sourcing rule, (i.e., because a portion of the equity award vested while he/she was on business travel in the US). In such cases, the employer of the business traveler will have an obligation to withhold the US federal income tax due.

However, a non-US resident employee on a business trip will be exempt from US federal income taxation on compensation for personal services performed in the US if the individual qualifies as a “short-term business visitor” under Sections 861(a)(3) or 864(b)(1) of the US Internal Revenue Code, or if the employee is a resident of a US treaty country and meets the tax exemption requirements of the treaty for individuals employed in the US for a short period. The conditions that must be satisfied for either exemption to apply generally require an assessment of the individual’s length of stay in the United States, the amount of compensation paid to the individual while in the United States and the nationality and/or business location of the employer. If an exemption applies, the employee should provide appropriate documentation to their non-US employer, including IRS Form 8233 if a tax treaty exemption is relied on to avoid US income tax withholding obligations.

The situation with respect to FICA tax for short-term business visitors to the US is less defined, as the US Internal Revenue Code does not contain a specific exemption from FICA taxes for individuals temporarily performing services within the country. In the absence of an applicable social security Totalization Agreement, technically, FICA taxes will apply to a non-US resident employee on a business trip in the US, even if for only one day, and notwithstanding that the employer may have no office or other place of business in the country.

If the individual is from one of the 30 countries with which (as of the date of publication) the US has a social security Totalization Agreement, there should be an exemption from FICA tax under the temporary assignment provisions of such Totalization Agreement, provided that the employee’s wages (including equity award income) earned while temporarily working in the US are subject to social security taxes in their home country. If a Totalization Agreement does not apply, it may be possible to take the position that the treaty implicitly provides for an exemption from FICA taxes, depending on the treaty if there is an income tax treaty between the US and the country of which the employee is a resident.

US state taxes also need to be considered in any US-inbound transfer scenario. Although it is highly unlikely that non-US residents on short-term business trips would be considered residents of the applicable state for income tax purposes, some states may tax the individual’s compensation, including equity award compensation, if the employee performed services in the state. Additionally, not all states recognize US federal income tax treaty exemptions or foreign tax credit provisions.

Therefore, before a non-US resident is sent on a short-term business trip to the US, it is important to confirm the extent to which the individual may be subject to US federal income tax, state tax and/or FICA tax. Assuming that an exemption is available, the necessary steps must be taken to rely on such exemption. Presuming US income and/or social security tax applies to income earned by the non-US resident during the business trip, to the extent that the individual holds stock options or other equity awards that have partially vested during such period, a tracking system needs to be established to ensure that appropriate taxes are paid when the individual ultimately realizes the income from the equity award (e.g., when exercising the stock option, or exercising/vesting in such other form of equity award) after departing the US.

Similar considerations will apply when a US resident is sent on a business trip to another country, depending on the local tax laws of that country and whether or not such country has entered into a tax treaty or social security Totalization Agreement with the US. An added complexity is that each country may have its own method of sourcing the income an employee acquires from equity awards for national income tax purposes. Many countries (including the US, as discussed above) broadly follow the model propounded by the Organization for Economic Co-operation and Development, which advocates sourcing the income employees earn upon exercise of a stock option (or similar award) between countries based on the work days spent in each country during the vesting period. However, some adopt their own variation of the rule (e.g., grant to exercise apportionment), while others apply unique rules that may lead to taxation of the entire award in the country in which the employee worked at the grant date, or on the exercise date depending on the circumstances. In addition, some countries tax equity awards at entirely different times than the US (for example, options may be taxed at grant in Belgium or at sale in Israel), further complicating the allocation of the income and the availability of foreign tax credit relief where double taxation applies.

Training

The tax treatment of equity awards granted to non-US residents coming to the US for training assignments will depend on a number of factors, including the immigration status of the individual and whether the entity that granted the equity awards qualifies as a foreign employer under the US Internal Revenue Code.

However, a threshold question for federal income tax purposes is whether the equity awards continue to vest (i.e., be earned and considered US-source taxable income) during the training assignment, which in turn depends upon the terms of the applicable stock plan. If, under the plan terms, a period spent in training is not considered continued employment for vesting purposes and the vesting of the award is therefore suspended for the duration of the assignment, US federal income taxes should not apply to any portion of the income the employee ultimately receives from the equity award.

For the purposes of the discussion below, it has been assumed that an individual on a US training assignment holds a J-1 exchange visitor visa, which allows for paid business training assignments for periods of up to 18 months, and that the vesting of the individual’s equity awards is not suspended during the assignment.

Under Section 872(b)(3) of the US Internal Revenue Code, a special federal income tax exemption applies to compensation paid by a “foreign employer” to a J-1 visa holder for the period he/she is temporarily in the US under J-1 visa status. For this purpose, a “Foreign Employer” can be defined to include a non-resident alien individual, a foreign partnership or foreign corporation, or a branch or place of business maintained in a foreign country by a US domestic corporation, US domestic partnership, or US citizen or resident.

Thus, to determine the extent to which equity award income earned by a J-1 visa holder while in the US is subject to US federal income tax, it is necessary to identify whether the entity that granted and bears the cost of the equity award is a Foreign Employer, under the above definition. If this is the case, any income the individual receives from the equity award should be exempt from US federal income tax, notwithstanding that the individual spent a portion of the period over which the award vested employed within the US.

On the other hand, US federal income tax would apply if, for example, the equity award was granted by a US corporation to an employee of one of its foreign subsidiaries, which subsequently sent the employee on a training assignment under J-1 visa status. This is because the income from the equity award that has been granted by the US parent corporation cannot be considered to have been paid by a Foreign Employer as required under the relevant US Internal Revenue Code tax exemption.

With regard to US FICA taxes, the situation is generally more straightforward since non-resident alien trainees temporarily present in the US under J-1 visa status are exempt from Social Security and Medicare taxes on wages paid to them for services performed within the US. This is as long as such services are permitted by the US Citizenship and Immigration Services and are performed to carry out the purposes for which the trainees were admitted to the United States. Therefore, it is likely that any income, including equity award income, an individual under J-1 status may receive during a US training assignment will be exempt from FICA taxes.

As with individuals in the US on short-term business trips, state taxes should also be considered.

Employment Assignments

The international employment assignment context is the key area in which multinational employers need to have controls and procedures in place to track and pay required US and non-US income and social security taxes on equity award income.

**US-inbound Assignments**

Subject to the terms of any applicable tax treaty, non-US resident employees coming on long-term employment assignments to the US (e.g., more than six months) will likely become US tax residents and therefore be subject to federal income taxes and potentially subject to FICA taxes and state and local taxes on all of their income, including equity award income, from both US and non-US sources (please refer to the “Income Tax and Social Insurance” portion of this section of the handbook for further details on attaining US tax residency). However, the challenge with respect to equity award income, (in contrast to regular salary) is that it is generally attributable to all countries in which the award-holder has been employed over the period between the grant and vesting of the relevant award, and may be taxable in such other jurisdictions under non-US sourcing rules. Note that different stock option sourcing rules apply under certain US tax treaties (e.g., with Canada, Japan and the UK, which apply a grant to exercise sourcing model), and under local laws of countries outside the US.

The result is that employees transferring into the US holding equity awards will likely be subject to federal income tax withholding on all income they receive from the awards while they are resident in the US. This is in addition to being subject to non-US taxes and possibly to withholding on at least a portion of the same income, subject to any relief that may later be available under the terms of an applicable tax treaty.

In addition, in the absence of a social security Totalization Agreement between the US and the non-US resident’s home country (or if there is a Totalization Agreement and the transfer to the US is for more than five years), with limited exceptions, FICA taxes will apply to the equity award income. Where a non-US resident is from a Totalization Agreement country (with the exception of Italy) and is transferred to the US for a period of five years or less, FICA taxes generally will not apply, provided that the individual has obtained a Certificate of Coverage from the home country social security authorities (confirming that they remain subject to the home country social security system) and furnished it to the US employer. Please refer to the “Income Tax and Social Insurance” portion of this section of the handbook for further information on US FICA tax considerations.

Furthermore, although rules will vary depending on the particular US state in which the transferred employee is employed, in cases where an individual is transferred to work in the US on a long-term or indefinite basis, it is likely that state taxes will apply to the individual’s income, including equity award income. Some states, including California and New York, have specific rules governing the taxation of equity award income partially earned within the state (and are focusing on this income from an audit standpoint), while many others have no specific rules and are therefore resorting to general principles is required to assess the tax liabilities.

On the regulatory side, if additional stock options or other equity awards will be offered to the US-inbound employee while they are in the US, the issuer must ensure that the offer of the securities complies with US securities laws. At the federal level, the shares offered under the equity plan will need to be registered with the US SEC or determined exempt from registration. The shares will also need to be registered or qualified as exempt from registration at the state level based on the state in which the employee is resident. In addition, it is necessary to ensure that the resale of shares by the employee is permissible within the US under applicable federal and state securities law registrations or exemptions.

**US-outbound Assignments**

Since US federal income tax applies to all income earned by US citizens and permanent residents (i.e., green card holders) anywhere in the world, equal if not greater challenges are presented when a US employer transfers a US citizen or permanent resident employee to work outside of the US. Irrespective of the fact that such outbound employees may, under applicable local tax laws, become a tax resident of and fully subject to income tax in the country to which they are transferred, in the absence of an exception under the US Internal Revenue Code, federal income tax withholding and reporting obligations will apply to all of the income earned by the transferred employees.

An exclusion from US federal tax applies under Section 911 of the US Internal Revenue Code for a certain amount of foreign income earned by a US citizen or resident (up to USD 108,700 for 2021). However, this exclusion is often not useful in the equity award context as the individual’s salary income alone surpasses this threshold (this foreign earned income exclusion is discussed in more depth in the “Income Tax and Social Insurance” portion of this section of the handbook).

An exception from US federal tax withholding that is useful for equity award income applies under Section 3401(a)(8)(A)(ii) of the US Internal Revenue Code where, at the time of payment, a US citizen’s foreign-source equity award income is subject to mandatory foreign tax withholding (this varies by country and, in some cases, by whether the local employer entity bears the cost of the equity award). To the extent foreign tax withholding is required on the foreign-source portion of the equity award income, US federal withholding is not required. Importantly, this US tax withholding exemption applies only to US citizens and not to US legal permanent residents, or others subject to US taxation, which may increase the administrative complexity of applying the exception on a broad basis.

Another exception to US federal tax withholding on foreign-source income may apply under the foreign tax credit provisions of Section 901(b) of the US Internal Revenue Code, provided that the transferred employee has indicated eligibility for a foreign tax credit on Form W-4. However, for equity award purposes, an important consequence of relying on this exception is that it is no longer possible to treat the equity award income as supplemental wages, subject to flat rate withholding at 22% to the extent the employee’s supplemental wages for the year do not exceed USD 1 million (and at 37% (2021) for amounts in excess of this threshold). Instead, US federal taxes must be withheld at the individual’s marginal tax withholding rate. Thus, depending on the relative amounts of US-source and foreign-source equity award income, the use of this withholding exception may not ultimately reduce the total amount of US taxes required to be withheld. In sum, the application of this exception must be carefully reviewed on a case-by-case basis (for further discussion of foreign tax credit, please refer to the “Income Tax and Social Insurance” portion of this section of the handbook).

Regardless of whether a US tax withholding exemption applies to all or a portion of a US-outbound employee’s equity award income, the employee must report the entire income on their Form W-2 for the applicable year if the employee is a US citizen or resident (including a green card holder).

If an individual employee is subject to double tax on equity award income as a result of withholding by their employer or former employer in two or more countries, relief may be available under the terms of an applicable tax treaty. However, that may be little comfort to the employee when almost all of the proceeds from, for example, a stock option exercise are initially withheld to meet multi-country tax obligations.

US FICA tax may also apply to the individual’s equity award and other income depending on the outbound US citizen or permanent resident’s employer entity and the existence of a totalization agreement between the United States and the country to which the individual is transferred.

In the absence of a Totalization Agreement, where a US citizen or resident is employed outside the US by an American Employer (e.g., a branch of a US corporation), US FICA taxes apply and must be withheld from the individual’s income, including equity award income.

If a Totalization Agreement applies and an individual’s equity award income would otherwise be subject to non-US social security taxes, US FICA taxes will generally no longer apply if the transfer is for more than five years (although there are some variations depending on the terms of the applicable Totalization Agreement).

In the US-outbound context, it is important to consider equity award income separately from salary. This is because a Totalization Agreement will not apply in the absence of double social security taxation, and equity award income paid by a US parent company to employees working at a subsidiary or affiliate outside the US is sometimes not subject to local country social security taxes, while salary is rarely (if ever) so exempt. Unlike federal income tax regulations, FICA regulations provide no basis for apportionment of multi-year compensation such as equity award income. This can increase the administrative complexity of meeting US withholding obligations in cases where it is possible to apportion income for income tax purposes.

**Solutions to Double Tax Issues**

To ease the potential tax burden of internationally mobile employees and to encourage employees to take business-necessary international assignments, most multinational employers have a tax equalization or tax protection policy (at least for certain employees, e.g., executive-level employees). These policies ensure that, from a tax standpoint, an international employment assignment is at least tax neutral and, in the case of protection programs, potentially tax favorable for the assignee.

Under a typical equalization policy, tax-equalized employees on foreign assignment will pay approximately the same amount of income and social security taxes that they would have paid had they remained in the US or their home country, with the employer paying any taxes that exceed this amount, and the employee reimbursing the employer if the amount of taxes they actually pay is less than their home country tax liability would have been. A tax protection policy operates in substantially the same way, with the key difference being that the employee does not have to reimburse the employer if their actual tax liability is less than the home country liability.

**Developing an Approach to Compliance**

Given the complexity of the foregoing rules, employers need to collect information and develop systems that will enable them to track and calculate the amount of the equity award income subject to taxation and, potentially, to employer withholding and reporting obligations in each applicable jurisdiction, as well as the extent to which exemptions from US federal tax income and FICA tax withholding may apply in different employment transfer scenarios prior to sending employees holding equity awards on employment assignments to or from the US.

An essential component of any compliance model is a reliable data collection system to gather and monitor key details that will be useful in determining the US and foreign tax and social security treatment of a given transferee. At a minimum, such details include:

The individual’s citizenship

US or foreign permanent residency status

US or foreign visa status

Time spent in each country during the periods over which the individual’s equity awards have vested

Whether the individual’s employment transfer is intended to be on a short- or long-term basis (including if it will be for more or less than five years)

Additionally, it is necessary to track whether the entity (or entities employing) the individual outside the US are US or foreign corporations and, if a US corporation, the state of the entity’s incorporation for US FICA tax and, in some cases, state social tax purposes for US-outbound employees.

Where a tax equalization or tax protection policy exists and income from equity awards is covered under the policy (some policies cover regular wages or other specified items of compensation only), it is necessary to be able to separately track the amount of equity award income paid to tax-equalized/tax-protected employees and calculate and pay both the US and foreign taxes actually due based on the individual’s residency and/or citizenship status and the amount of home country taxes that would have been payable had the individual not gone on assignment.

For companies with a large internationally mobile population, it is important to track patterns of international transfer, develop models that will generally apply to common inter-company transfers (e.g., US to UK or India to US) and create assumptions about employment assignments and categories of employees that will facilitate the development of a system that is both compliant and workable.

Other Comments

Compliance with income and social security tax requirements is the key concern when equity award-holder employees transfer to and from the US.

However, regulatory considerations should not be overlooked. To the extent that equity awards are offered to employees while on international assignment within or outside the US, issuers of such awards must ensure that they comply with any securities law prospectus, registration or exemption filings and any applicable foreign exchange control, labor law, data privacy or other filings that may be necessary to offer equity awards under the local law of the country in which the assigned employee is resident. Compliance with the requirements of local tax-qualified regimes may also be desirable.

Furthermore, where employees are transferred to a new country after an equity award grant date, particularly where such transfer is on a long-term basis, it may be necessary or desirable to modify the terms of such award to comply with local law or gain the benefit of a favorable local tax regime. It is important to structure equity award grants to allow for flexibility to address legal issues that may arise should an employee be relocated after the grant date while bearing in mind accounting issues and plan limitations. For companies making new grants of equity awards on a global basis, a useful best practice is to adopt a single global form of award agreement that includes a country-specific terms appendix and a relocation provision. Then, if an award-holder goes on an international assignment after the grant date, the agreement’s relocation provision gives the issuer authority to apply the terms set forth in the appendix to the agreement for the country of transfer (to the extent necessary to comply with applicable laws or administer the grant).

***Further Information***

The Global Equity Services Practice, supported by colleagues advising on the taxation of expatriate assignments, works in coordination with the Global Immigration and Mobility Practice on global mobility assignments. GES practitioners provide streamlined advice on both the US and non-US tax, social security and legal aspects of short- and long-term international employment transfers in the equity awards context. They also assist multinational companies in developing an approach to global equity compensation tax liabilities that combines the degree of legal protection and operating flexibility most appropriate to the interests of the relevant company.

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