

Structuring Expatriate Postings

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Multinationals that send expatriates abroad too often either ignore the issue of how best to structure the assignment, or struggle with expat structuring problems.

It might seem that there must be one single best way to structure an intracompany expatriate posting. But there is not. Even within a single multinational, different expat assignments need to get structured in different ways, because small differences among expat postings can compel different assignment structures: Your last expat may have gone to a country where you have an up-and-running affiliate but your next expat may be off to a jurisdiction where you have no on-the-ground infrastructure. Or your last expat may have participated in your company expat program but your next expat may instigate a transfer for personal reasons that make him ineligible for a company package.

There are five possible expat assignment structures (plus hybrids among them):

1. Home-country-affiliate employed and paid
2. Home-country-affiliate employed/host-country-affiliate paid
3. Localized
4. Localized with “hibernating” home-country affiliate agreement
5. Dual employment contract

Five Expatriate Structures

Type of expatriate	Structure	Tax/payroll issues (beyond tax/social security treaties)	Inter-affiliate agreement a best practice?	Other issues
1. Home-country-affiliate employed and paid	Expat remains on home-country-affiliate payroll; works in host country; inter-affiliate reimbursement chargebacks sometimes used	Expat is taxed in host country; home-country affiliate may invoke social security totalization treaty when available	Yes	Possible “permanent establishment” for home-country affiliate in host country; possible deemed dividend or other deemed payment between home-country affiliate and host-country affiliate if value of services is not reimbursed
2. Home-country-affiliate employed/ host-country affiliate paid	Expat’s employer is home-country affiliate; pay is delivered by host-country affiliate	Expat is taxed in host-country; host-country affiliate makes mandatory withholdings. Home-country affiliate may invoke social security totalization agreement when available	Essential	Possible “dual employer” problem for host-country affiliate (home-country affiliate deemed “doing business in” host country because it employs someone there)
3. Localized (host-country-affiliate employed and paid)	Expat resigns from home-country affiliate, simultaneously hired by host-country affiliate	Expat taxed in host country; host-country affiliate makes mandatory withholdings	No	Undesirable to expat (unless no expectation of repatriation); seniority recognition and social security accrual issues
4. Localized with “hibernating” home-country affiliate agreement	Home-country employment agreement expressly suspended until repatriation; expat hired by host country entity	Expat taxed in host country; possible dual-jurisdiction tax ramifications; some home-country (e.g. Brazil) payroll contribution obligations persist	Yes	Expat has extra (home-country contract) rights when terminated or repatriated, significantly complicating terminations
5. Dual employment contract (paid on either home or host-country payroll, or both)	Expat has two simultaneous employment agreements: one with home-country affiliate, one with host-country affiliate; may be split pay, or intra-affiliate chargebacks	May be tax benefits, but there will be tax and dual payroll contribution complexities: Seek dual-jurisdiction tax advice	Essential	Significant permanent establishment risk for home-country affiliate. Significant legal complications on separation: If terminated or repatriated, expat may invoke legal rights under both home- and host-country laws

Which of the five structures works best for a given expat’s assignment depends on the circumstances. In posting an expat abroad and selecting the ideal structure, be strategic and factor in the concepts in play. Eliminate those structures that do not make sense this time. Of the structures remaining, select the one most business-appropriate.

- For example, one expat structure—home-country-affiliate employed and paid—is usually viable only: where a home- country employer entity already has a legal presence or permanent establishment in the host country; where a host-country employer entity is available to issue a shadow payroll; and where the two employer entities can work out an accommodation as to dual/co-employment. Therefore, never select the “home-country-affiliate employed and paid” structure without accounting for the concepts of permanent establishment, payroll compliance, and dual/co-employment.

Here are seven key concepts to consider before selecting among the expatriate assignment structures:

1. Expatriate type

An expatriate employee is someone originally hired by, and working for, an employer in one country who later gets assigned to work abroad for that same employer, or an affiliate. In structuring an expat assignment, distinguish among the various types of expats and quasi-expats:

“Stealth expat”

Not all *actual* expatriates get to participate in a multinational’s expat (benefits) program. Unfortunately, corporate jargon inside many companies reserves the “expatriate” label only for all-the- bells-and-whistles expats who qualify for an expensive company expat package. This usage can lull a multinational into overlooking or misclassifying actual expats who, for whatever reason, are ineligible for its expat program (examples: *trailing spouses* of other companies’ expats; *telecommuters* working

abroad for personal reasons; *stealth expats* whose place of employment shifted abroad by default, such as after extending a long business trip, without the employer's legal/payroll/HR teams acknowledging the move).

Inpatriate and third-country national

An inpatriate is an expat coming from a foreign country to work at headquarters. A third-country national is an expat from a foreign office (not headquarters) assigned to some other foreign office.

Career expat

A career expat is an expat serially assigned from one overseas posting to the next, as opposed to a "one-off" expat posted abroad on a single assignment.

Seconded

An expat on "secondment" remains employed by, and often paid by, the home-country nominal employer entity, while lent out to (rendering services for) a different beneficial employer entity overseas (which may or may not be an affiliate of the nominal employer).

Transferee/"localized" expat

An expat transferee is an employee moved overseas, often rehired by a local employer affiliate, without any lingering right to work in the former home country. An expat transferee is said to be "localized" with the new employer (or office) overseas.

Sometimes the parties intend a localization to be temporary, with the employee expecting later to transfer back, re-localized in the original location.

Opinionated expat

In some cases, the biggest problem with a multinational's ideal expat structure is expat resistance. For obvious reasons, expats prefer structures that minimize personal income tax exposure in both home and host countries. Expat candidates may resist being localized and being seconded to a manpower services agency. Some expats demand untaxed offshore wage payments.

Quasi-expat

A quasi-expat is an internationally-mobile local employee sometimes confused for an expat. For example, a *foreign hire* is a new hire who happened to get hired out of a different country than the one where the job is based. A foreign hire is a local employee and need not be structured as an expat—even if the compensation arrangement is to pay expat-like benefits and to facilitate a visa/work permit. A *long-business-trip traveler* works abroad temporarily on a long business trip, but for a short enough period that local host-country law recognizes the “place of employment” remaining the home country.

2. Legal presence/permanent establishment

When structuring expat assignments multinationals should consider permanent establishment issues.

A “permanent establishment” is a corporate tax presence imposed by law on an entity held to be doing business locally. A permanent establishment comes up when the home-country entity has no formal corporate presence in the host country (is not registered as a branch, not incorporated, not licensed to do business locally), but ends up transacting business in the host country through the acts of its expat. Once the expat's activities on behalf of the home-country employer trigger a jurisdiction's definition of "doing business in" country, the home-country employer is deemed to have a local "permanent establishment," a *de facto* corporate presence. This finding carries with it legal obligations to: register with the corporate registry (local equivalent of a US state secretary of state's office); file local corporate tax returns; get a local taxpayer identification number (and, if the organization is a non-profit, get local non-profit status).

The expat challenge is where this “doing business” is employing an expat in a jurisdiction where the employer otherwise does not operate. Imagine for example a German corporation employing a full-time, profit-generating expat in Chicago but otherwise doing no business stateside; even if that expat telecommutes and works solely on German matters with no connection to US commerce, the US IRS and Illinois agencies could argue the German employer does business in Illinois simply by employing this person—and so should register with the Illinois secretary of state and file corporate tax returns. It works the same way abroad.

3. Payroll compliance and offshore wage payments

Structure expat assignments to facilitate payroll compliance and avoid illegal offshore wage payments. Perhaps every country imposes payroll laws that reach employers of staff working locally, such as laws requiring employer reporting/withholding/ contributions on

behalf of employees to local tax authorities and social security agencies/funds. Local payroll laws almost always reach inbound expats. (US payroll laws, for example, reach in-pats working stateside, and it works the same way abroad.) Local payroll laws have the effect of banning offshore wage payments where a foreign (home-country) employer/payor lacks local (host-country) registrations/taxpayer identification numbers and so cannot comply. Registering a foreign (home-country) employer/ payor entity for host-country payroll only can be surprisingly complex; for example, enrolling a US employer corporation not otherwise licensed to do business in Mexico with Mexico's tax, social security and housing fund agencies can take more than six months as the various Mexican agencies pose questions, schedule in-person meetings, and question US corporate status.

Local law accommodation

Exceptions to payroll laws for expats are rare, but some countries offer special accommodations for limited classes of incoming foreign temporary employees (like diplomats, military, NGOs, non-profits, reporters) to work in-country while paid offshore on home-country payroll.

Shadow payroll and intra-company chargebacks

When an expat's home-country employer continues to pay an expat offshore even though it cannot comply with host-country payroll laws for lack of registrations, one strategy is to arrange for some host-country-registered entity (often an affiliate) to issue a "shadow payroll" showing compensation as if paid in-country, and otherwise complying

with host-country payroll laws. The entities may then use an intra-company chargeback (intra-affiliate payment) to reconcile payroll expenditures.

Split payroll

Sometimes the host country entity pays an expat one chunk of compensation while the home-country entity pays another chunk. Beware: The offshore payment must comply with host-country payroll laws. Unless the expat actually “moonlights,” working two jobs in two countries, split payrolls can be a red flag.

Social security totalization treaty

A social security totalization treaty is a bilateral treaty allowing an expatriate to continue on the home-country social security system, usually for up to five years, as the employers register and continue to make contributions. As of Dec 2012, the U.S. Social Security Administration website said the U.S. is party to 24 of these treaties. Contrary to a common misunderstanding, these treaties implicate social security only and do not reach *income tax* reporting/withholding.

“Flying under the radar”

Many expats work in overseas host countries while being paid, illegally, offshore. Until an illegal offshore pay arrangement catches the attention of some host-country tax/social security/labor agency or gets litigated in a local labor court, it might euphemistically be said to “fly under the radar” of host-country payroll enforcers.

4. Dual/co-employment

In the expat context, a dual/co-employment issue arises when home-country and host-country nominal and beneficial employer entities stay involved in an expat or secondment arrangement, such as in compensating the expat. Some dual/co-employment arrangements get structured explicitly while others are after-the-fact determinations disputed by unwilling co-employers.

“Hibernating” agreement

A “hibernating” expat employment agreement is an expat’s legacy home-country employment agreement that predates the expat assignment and that, during an assignment, gets suspended by and subordinated under the expat assignment arrangement. Hibernating home-country agreements “spring back to life” upon expat termination (or repatriation), often complicating separations by introducing the dual/co-employment issue.

5. Global employment company [GEC]

A GEC is a multinational subsidiary (sometimes incorporated in Switzerland) established to employ a team of career expatriates. A GEC can greatly simplify expat *pension and benefits administration*, but—contrary to a widespread misunderstanding—a GEC is more an administrative convenience than a “magic bullet” solution to expat legal/structural challenges.

6. Visa/work permit

Every foreign placement must comply with host-country immigration law. Except where an expat is a host-country citizen, this almost invariably requires getting a local visa or

work permit. The expat structure issue here is *visa sponsor*: A home-country employer entity not registered in the host country will rarely be eligible to sponsor a visa or work permit, and for this reason alone may not be an appropriate employer entity.

7. Secondment (expat) agreement

There are two types of secondment, or expat, agreement. The first is an *expat assignment agreement* between an expat and the employer (home-country entity, host-country entity, or both). The second is an *inter-affiliate assignment agreement* between a home-country employer entity and a host-country affiliate entity (the expat is not a party). As appropriate, structure and document an expat assignment using one or both agreements.

Employer control

In a secondment, usually the nominal employer entity, not the beneficial employer entity, wields ultimate power to make employment decisions such as setting pay/benefits, imposing discipline/termination, and determining the duration of the secondment. In crafting secondment agreements, factor in these balance of power issues.

Choice-of-law clause

As soon as an expat's place of employment becomes a new country, local host-country employee protection laws (laws on work hours/overtime, vacation/holidays, wages/benefits, payroll, health/safety, unions, discrimination/harassment, severance pay, etc.) generally protect the expat by force of public policy. The problem with an employment-context choice-of-law clause is that it implicates tougher employment laws of the selected jurisdiction without blocking

the mandatory application of tougher employment protection laws which apply by force of public policy in the host jurisdiction. Both sets of laws may end up protecting the employee. The employee may get to “cherry pick” whoever rules offer better protections. This analysis generally applies regardless of expat structure, so this choice-of-law issue often drops out of the expat structure selection analysis, unless where an exception applies, such as in China, when the choice of law might play a role in the structuring agreements.