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Navigating BEPS: Keeping track of the tax changes for internationally mobile employees

Across a number of countries, the way internationally mobile employees are taxed is being shaken-up. This follows the G20/OECD-led Base Erosion and Profit Shifting (BEPS) Action Plan recommendations set out earlier this year.

This huge package of reforms is designed to bring tax liabilities more closely into line with the economic 'substance' of where and how value is created. For internationally mobile employees specifically, this may mean that corporate tax liabilities can arise in locations where the employee carries out activities, rather than just where they are legally employed or on the payroll.

The potential impact includes a sharp increase in the number of jurisdictions in which your company may be deemed to have a taxable presence (permanent establishment) and the complex tax registration, calculation and reporting demands that go with this. Failure to get to grips with the shift will increase your risk of tax investigation, dispute, penalties and potential reputational damage.

Putting tax management for internationally mobile employees on a solid footing needs a more systematic approach to workforce tracking, strategic employee deployment, determination of home locations for employees with key roles, and tax filing for staff working across multiple markets. How can your business get up to speed?

Who's in the BEPS net?

The OECD's BEPS Action Plan provides a comprehensive international framework for corporate taxation for businesses. While the guidance and associated requirements are set to cover around 90% of global corporate revenues, certain aspects of the framework are aimed at the largest multi-national enterprises (MNEs). For example the Country by Country Reporting (CbC) template will only be required to be completed by groups with a turnover in excess of €750m. However the OECD believes that 85-90% of multinational enterprises (MNEs) would be exempt from CbC.[1] Crucially, however, the OECD doesn't set laws or sign tax treaties – governments do. So there's bound to be a significant variation in the timing of implementation and interpretation of how the guidance is applied.[2]

If we look specifically at internationally mobile employees, a lot more activities are going to come under tax authority scrutiny. Even a field agent involved in the sales process may be deemed to be a permanent establishment (ie a market where your business has a taxable presence), for example.

While the businesses we're advising on BEPS range in size, the relatively smaller enterprises can often face the biggest challenges as they don't have the tax management expertise and infrastructure to know whether they fall in the net, how they will be affected and how to deal with the strategic and operational implications.

Globalisation continues to boost the numbers of people working across international borders. An internationally mobile workforce not only plays a key role in driving business expansion, but also strengthening the agility and control of fixed costs that are vital in today's fast moving business environment. They stretch from project workers, international assignees and executives with global or regional remits to a constantly roving group of specialist sales representatives and fly-in and fly-out business travellers. More and more people also now live in one country and work in another.

While management of this workforce may be well-embedded within large groups, smaller organisations with international operations often have less oversight over who is being deployed, where and how. They may also be taking initial steps into fast growth markets or rely on sales agents and executives working across multiple territories, which can bring greater tax risk and exposure.

What's changing?

The need to bring tax calculation and collection closer into line with where and how value is created as part of the BEPS Actions complicates how the activities of internationally mobile employees are treated for tax purposes and the level of scrutiny they are likely to face. Adding to the challenges are the increase in tax audit activity internationally, growing investment in tax audit capabilities by revenue authorities and new channels of bi- and multilateral information sharing, which will heighten the spotlight on your internationally mobile employees. Key considerations for your business include:

Permanent establishment

Changes to tax rules resulting from the BEPS Action Plan increase the range of activities that fall within the definition of a permanent establishment.[3]

In relation to internationally mobile employees, even relatively brief stopovers and sales trips could now trigger a permanent establishment designation, resulting in unexpected corporate tax liabilities as profits are pulled into tax in overseas jurisdictions.

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[1] OECD BEPS Project Action 13: Guidance on the Implementation of Transfer Pricing Documentation and Country-by-Country Reporting, 2015 (http://www.oecd.org/ctp/beps-action-13-guidance-implementation-tp-documentation-cbc-reporting.pdf)

[2] Different jurisdictions have different thresholds to determine whether a business is designated as small, medium or large. Standard thresholds are usually based on Group turnover, balance sheet assets or number of employees. In the EU, for example, a small enterprise is one that has less than 50 employees and either less than €10m consolidated turnover or €10m on its consolidated balance sheet. A medium enterprise is one that has less than 250 employees and either less than €50m consolidated turnover or €43m on its consolidated balance sheet.

[3] Action 7 'Artificial avoidance of permanent establishment status'.

And administrative burdens may increase with your business needing to complete tax registrations and filing, and manage new or additional income or sales tax liabilities. For example, the definition of a permanent establishment has now been broadened to include activities that routinely lead to the conclusion of a contract rather than just the conclusion of the contract per se. This is designed to prevent companies from avoiding a permanent establishment status by ensuring that the final contract is signed offshore. The definition of what constitutes an independent agent has also been tightened up – if more than 90% of sales go through the agent, then he or she wouldn't be independent, for example.

Furthermore, it is also important to remember that creating a permanent establishment will typically mean internationally mobile employees are generating value in that location resulting in additional tax and payroll reporting requirements for both the business and the employees.

The key question for your business is do the activities of your internationally mobile employees create an extra set of permanent establishments and, if they do, where and how can this be managed and tracked?

Action:

You need to track the movement and operations of your internationally mobile workforce to determine whether the registration for tax purposes reflects the substance of their activities. To save time and expense on tracking these employees, use of the systems you already have is a starting point. They might include a central booking system for flights or perhaps each office requires individuals to sign in and out. Investment in specialist technology can allow for cost effective oversight and management, along with tracking tax exposure in real-time.

You may need to register in additional jurisdictions as a result of the assessment. And you would then need to establish filing capabilities and tax authority engagement in what could be multiple new jurisdictions. You may not have the resources or expertise to manage filing requirements in multiple jurisdictions, so outsourcing these operations can prove to be efficient, cost-effective and minimise risk.

Transparency

New CBC reporting requirements mean that if your company is within the BEPS threshold you will have to disclose how many people are working within a particular tax jurisdiction, together with additional information such as how much revenue is being generated in that country. When reporting the number of employees in each jurisdiction, we see potential difficulties in determining where employees should be counted in cases where dual contract and secondment agreements are in place.

The challenge for your business isn't just how to manage the reporting demands, but the risk of increased tax demands that could result from what you reveal.

Action:

CbC reporting imposes significant demands on data gathering, documentation and management review of disclosures. You'll probably need to make upgrades in systems and governance procedures – both locally and at group level. Also look at how the information in the CbC reporting may be interpreted and used by tax authorities, and what risks this opens up.

The starting point is disclosing the employees who are legally employed in the reporting jurisdiction, before reviewing whether any other employees who are legally employed abroad create value here (ie expats, visitors etc.). If they are creating value, but don't appear on the payroll, they could expose your company to a potential audit.

Heightened risk

BEPS heightens tax risk by increasing both the complexity and the scrutiny of the arrangements for internationally mobile employees. Do your tax arrangements and disclosures reflect the economic substance of your activities?

The risks are heightened by CbC reporting, enabling tax authorities to compare declared income and staff numbers with the tax paid in a particular jurisdiction. Tax authorities could challenge the absence of permanent establishment status or target what they see as a shortfall in tax revenues.

Action:

You need to assess and proactively manage the risks at both group and local level. Make sure you also educate employees, so that where potential risks arise, someone has reviewed the position to ensure that these are managed.

The move to risk-based audits means that companies with demonstrably better controls and processes are less likely to be investigated or face penalties. Clear and comprehensive documentation and policy justification are vital in assuring tax authorities that tax management and underlying assumptions are sound.

Strategic implications

The new rules have already led to significant shifts in either personnel or corporate registration for tax purposes. More are likely to follow.

Permanent establishments in new locations may affect overall corporate tax planning, impacting the marginal tax rate and in turn, overall financials, profits and return to shareholders.

Action:

Review your corporate structure in light of all the various impacts of BEPS to judge whether the structure should be expanded or adjusted, for example through the setting up of additional branches or legal entities.

And be clear about the tax triggers under BEPS so you can plan and manage the internationally mobile employee's base location, their movements, their activities and the compensation, expenses and benefits these entail in the most efficient way.

Communication between the functions responsible for employee movements and tax will help to ensure your business is aware of all local and global requirements when employees and directors move from country to country.

Apportioning value

If one of your employees goes to work on a secondment or project, the entity that permanently employs them may charge the host entity.

BEPS complicates the calculation of these charges through the need to ensure that transfer pricing is in line with value creation[4] (ie what's paid reflects the substance of the employees contribution). This is complicated further by the need to ensure that calculations reflect the expertise of the assignee and the intellectual property they 'transfer' in line with intangible value considerations within BEPS transfer pricing.

Action:

Charging for internationally mobile employees, along with transfer pricing more generally, will be an increasingly important requirement as a result of BEPS. Make sure that assignment management and transfer pricing are aligned. You're likely to require professional guidance and assistance to pull together your transfer pricing policy, as well as appropriate transfer pricing documents.

[4] Actions 8-10: Aligning transfer pricing outcomes with value creation

Aligning strategy, mobility and tax

The impact on your international mobile employees requires a strategic rather than just a narrow tax compliance response, making it a matter for your board as well as corporate tax. Internationally mobile employees may be seen as the responsibility of the tax function, human resources (HR), finance and also payroll. What's clear is that given the potential challenges involved, it takes a joined up effort and the availability of information and technical support to manage risk. Depending on the size and resources of your business, you may need to outsource some aspects of management, including tracking, tax analysis and the operationally demanding reporting and transfer pricing requirements. But you can't outsource the risks and responsibilities, so make sure that the strategic, operational and tax management of global mobility are closely co-ordinated.

Taking the stress out of tax management

Few components of international mobility are as complex as managing and negotiating the intricacies of cross-border travel. Against a backdrop of increased legislation, heightened revenue audit activity and information sharing, ensuring your business is managing risk and exposure on multiple levels across corporate tax, payroll withholding and individual tax exposure for your executives is a challenging task. Success relies on an understanding of the challenges unique to your organisation and a collaborative approach across your tax, finance, HR and payroll functions. Having clarity in responsibilities and the right solutions in place are key factors in ensuring your organisation and employees are complying with tax obligations internationally and that tracking is strategically aligned with the business' global growth objectives.

The impact of the BEPS Action Plan has raised the bar of managing internationally mobile employees further still. Our Global Mobility Services professionals and our international organisation can work with you to develop and implement the policies and processes; travel tracking and analytics solutions; alongside reporting and compliance, to make sure you are robust in managing your obligations. Leveraging technology that can manage your internationally mobile employee population and deliver insights on tax risk in real-time, your Grant Thornton team can partner with you to ensure you manage risk proactively and ensure that your business and your people are focussed on what matters most to you: your continued growth and success.

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