Implications of Automatic Exchange of Information and Base Erosion and Profits Shifting initiatives on global mobility of employees

It is never easy for companies to manage their globally mobile employees under today's evolving regulatory environment. These employees may be on short term or long term assignments in foreign locations and in some cases may even conduct frequent business trips in lieu of fixed term assignments. These employees are required to obtain proper immigration visas and often times the application processes and requirements are complex.

From a tax perspective, employer's and employee's tax filing requirements in both home and host locations should take into account domestic tax rules and double tax treaties (if available). Companies also need to manage their corporate tax risks in foreign locations as a result of the nature and duration of services rendered by these mobile employees. Implications in relation to social security schemes (or similar arrangements) also need to be addressed.

In order to increase transparency and better align taxation with value and profit creation, the Organization for Economic Cooperation and Development (OECD) has put forward two initiatives, namely the Automatic Exchange of Information (AEOI) and the Base Erosion and Profits Shifting (BEPS) project. Tax authorities across the globe are called to participate in these two initiatives, which have been endorsed by leaders of the G20 countries. Notwithstanding that the measures under AEOI and BEPS packages may be perceived as tax focused, there are wider implications affecting how companies manage their mobile employees. Indeed, ensuring that companies and their employees comply with the evolving regulatory requirements is increasingly important.

This article first outlines the key objectives under the frameworks on AEOI and BEPS, and looks into what the OCED is aiming to achieve. It also covers the implications of both AEOI and BEPS from a global mobility perspective, and explores the issues affecting both employees and employers. Finally, based on our observation in the market, we propose some potential solutions to help companies manage issues that may arise as a result of these OECD initiatives.

Automatic Exchange of Information (AEOI)

The concept

AEOI (also referred to as Common Reporting Standards (CRS)) forms part of the OECD's wider initiatives which are designed to improve global tax transparency. AEOI aims to achieve this by establishing a network of competent authority agreements which allow each participating jurisdiction to obtain information from its domestic financial institutions and exchange that information with respective jurisdictions on an automatic basis. The competent authority agreement specifies the details of information for exchange and its timing. In this regard, the AEOI framework is expected to encourage individuals to pay taxes correctly in countries where they are deemed to be tax residents as information is timely shared among global tax authorities.

The details

AEOI requires reportable financial institutions to report account details of reportable persons to the domestic tax authorities. The domestic tax authorities have an obligation to share these details with global tax authorities with whom either a multilateral or bilateral competent authority agreement is in place.

If we break down the above concept you will see the details of what it covers:

Reportable financial institution – this typically covers standard "banks" but also includes certain insurance companies, investment vehicles, and specified entities as well.

Account details – account details of a reportable person that are shared with the domestic tax authority include account balance, interest, dividends and proceeds from the sale of financial assets.

Reportable person – in terms of an individual, a reportable person is a tax resident in a reportable jurisdiction under the laws of that jurisdiction, while a reportable jurisdiction means it is a participant of the AEOI framework.

Reportable financial institutions are required to conduct due diligence exercises to confirm whether an account holder is a reportable person. As a part of the due diligence exercises, an account holder may be required to complete a self-certification form in which the account holder declares his or her jurisdiction(s) of tax residency. Depending on the local laws on AEOI enacted by jurisdictions, individuals may be subject to penalties or other punitive actions for providing incorrect information in the self-certification forms.

A self-certification form is also required to be updated when there is a change in an individual's circumstance, such as changes in addresses, and jurisdiction(s) of tax residency. Forms should be completed and submitted within 30 days of the changes of circumstance.

Competent authority agreement – About 100 countries have agreed to be part of the AEOI initiative. However in order to share the financial account information, each jurisdiction needs to enter into either multilateral or bilateral competent authority agreements with others to effect exchange of information. For example, as of May 2017, Hong Kong has entered into bilateral competent authority agreements with 11 AEOI participating jurisdictions whereas the earliest exchange of information will occur in 2018. Hong Kong is expected to increase its AEOI partners to 75 within 2017, although exchange of information with some of these AEOI partners will not take place until the relevant AEOI agreements have been signed with them.

Implications on global mobility

Under the AEOI framework, mobile employees who need to open bank accounts in foreign locations for payroll or other purposes will be required by financial institutions to complete self-certification forms. As part of this self-certification process, they have to state the place where they are deemed tax residents.

Tax residency can be a complex concept and it is possible for an individual to hold multiple residencies. Conversely, there are also cases where global workers hold no jurisdiction of tax residence.

For mobile employees who have been sent to work in foreign locations by their employers, the AEOI initiative raises the question of whether they have the proper technical knowledge to determine their jurisdictions of tax residencies. They may expect assistance from their employers in helping them to complete self-certification forms, thus confirming their tax jurisdictions of residencies.

From an employer's standpoint, the decision on whether or not to provide assistance to employees in completing the self-certification forms should not be made on an ad-hoc basis. Since there may be penalties imposed on incorrectly completed self-certification forms, companies (especially those with a significant population of mobile employees) should have clear mobility policies in place to confirm that it is the employees' responsibilities to complete the self-certification forms, and address whether support is provided by employers to assist employees in the completion process.

The Base Erosion and Profits Shifting (BEPS) project

BEPS refers to tax avoidance strategies in which profits are shifted artificially to no-tax or low-tax jurisdictions. Companies which adopt such tax avoidance strategies may then pay very little or no taxes when compared to the amount they would have to pay in the original location where the profits were earned. The OECD recognizes that this is not only morally questionable but also reduces the level of taxes paid in the country of origin, thus affecting its overall economic and social development. This is particularly prevalent in developing countries.

To combat this practice, the OECD has developed an initiative which brings together over 100 countries to deal with the issue of BEPS. Under the OECD's BEPS Action Plan, there are 15 actions and under each action, there are various recommended measures for tackling BEPS. These actions have been categorized by the OECD into three key themes: addressing substance, coherence of the international tax system, and transparency.

The details

Considering from a global mobility perspective, we look at the concept of building substance and the issue of permanent establishment under the OECD's BEPS project.

Building substance

As the focus on BEPS increases, there will be greater scrutiny by tax authorities to look at whether the location where companies report profits is also the location where the economic activities that generate those profits are performed. Economic substance is often built by, among other things, the presence of employees, the nature of duties rendered by them, and the value created by the work performed. As such, the concept of "shell" companies in which inappropriate amount of profits are reported will be under much greater attention as tax authorities look in details about the number and role of personnel employed in that location.

Permanent establishment

The concept of permanent establishment (PE) is also in the spotlight under the OECD's BEPS package. The issue of PE is of concern to organizations, as it can create both corporate and individual tax exposures in locations where the business does not have any entities set up. Historically, PE risk has been centred on the locations where final contracts were concluded. Under the new BEPS regulations, tax authorities will now look into where the activities leading up to the contract conclusion were carried out, to determine if a PE has been created in a location.

Implications on global mobility

As a result of the BEPS changes, there will be an increased focus on substance over contractual or legal arrangements. Companies should review their corporate structures to ensure that regional offices have adequate staff to support the profit levels reported through these entities. It is expected that companies will be looking to increase their employee numbers in key locations to build substance. It will be essential not only for companies to move personnel, but also to ensure they are filling positions with the correct skill sets. The positions and roles of staff will need to be sufficient in order to support the level of profits being reported.

In respect to managing PE risk, the tracking of business travellers will be key not only to monitor where they are travelling but also the activities they are doing. As significant corporate contracts tend to involve senior staff members, it is also critical that they are aware of the PE risks and the importance of keeping track of their business travel. Businesses often have mobility policies in place for traditional assignments but may not have any programmes in place for short term business travellers. The increased concerns regarding PE risk may therefore reinforce a company's focus to properly manage these groups of employees.

Possible solutions to address issues arising from AEOI and the BEPS project

The measures introduced under the BEPS project and AEOI create complex issues which have implications across a range of stakeholders within an organization. As such, companies are keen to gain an understanding of the topics and the implications these will have for them.

Below are examples of the challenges and solutions that companies are considering to help them address the global mobility implications of the BEPS and AEOI initiatives:

- Training

  As the above topics are complex and relatively new, many human resources and tax teams may not be familiar with the specifics. As many mobile employees will be impacted by these changes, they will often call HR with any inquiries. Therefore, it is important that HR teams and other related personnel are up to speed on the topics. In order to address this need, companies are seeking group training on these topics to ensure their relevant teams have enough knowledge and also have the chance to establish what these may mean for their companies.

- Policies implementation and policy review

  The AEOI in particular will impact mobile employees as they will now be required to complete self-certification forms in order to open accounts with reportable financial institutions (such as banks) while on assignment. The declaration of tax residency in the self-certification forms requires employees to thoughtfully consider their facts and circumstances, such as domicile, nationality, the number of days spent in a jurisdiction, and other factors. If these forms are incorrectly completed, there may be penalties imposed on the individuals. As a result, it is recommended that companies review their existing mobility policies and decide how the policies should be updated to address the impact of AEOI, for example, whether or not the companies will provide support to mobile employees for completion of the self-certification forms.

  In respect to PE monitoring, companies may not have any mobility policies or tracking tools in place for short term assignees and business travellers. Due to the increased PE risk on the companies from the BEPS changes, greater focus should be put on these populations. In particular, companies should look into having comprehensive systems and robust processes to approve business travels, track the nature of activities carried out by mobile employees, identify the locations where the services are performed, and comply with the necessary tax, immigration and other mobility-related requirements on time.

- Communications with employees

  While it is important for internal tax and HR teams to be fully informed on these new changes, it is equally important that affected employee groups are also fully informed. This not only ensures they are aware of policies and processes they need to follow, but also improves the overall assignment experience for employees who are working internationally.

As such, companies are looking to enhance communications with key employee groups regarding companies' updated policies in addressing issues arising from AEOI and the BEPS project, and ensure they are aware of their respective roles and responsibilities.

Conclusion

The introduction of the BEPS project and AEOI marks some of the greatest changes in the international tax landscape for a number of years. The behaviour of tax authorities will likely be changed as global tax transparency promotes greater scrutiny to affirm that both corporate and individual taxpayers pay the right amount of tax in the right locations.

Companies will need to review whether they have the right number of employees with the right skill sets to work in locations where profits are aligned with taxes paid. In many cases, this alignment of talent and profits leads to secondment of employees or arrangement of frequent business travellers. When there is a need to mobilize their talents across the globe, employers and employees need to ensure they are fully compliant with respective regulatory requirements in both home and host locations, such as individual income tax filings, immigration visas, and contributions to social security schemes.

Companies are recommended to keep abreast of the updates on rules relating to BEPS and AEOI and prepare for the changes, and to proactively manage any costly risks. Various stakeholders within business organizations should get involved as early as possible and collaboratively take appropriate actions to ensure compliance with requirements brought by the BEPS and AEOI initiatives from a global mobility perspective.

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