Transfer Pricing - Filipa Correia, Crowe Valente, Italy

Introduction

Tax issues and global mobility go hand in hand. There can be tax matters for the employee and for the employer. The corporate tax implications (tax matters that relate to the employer entities) are generally less well understood in the world of Mobility/HR, than the payroll and employee and employer issues.

Within the corporate tax area is transfer pricing. In the context of employee mobility, this is an area that concerns itself with how the cost of employees is borne and cross charged within a group. Mobility often has to work in partnership with finance and tax departments around this issue.

A high level of understanding is therefore essential for mobility professionals. The issue impacts what costs are allowed, or should be deducted, to determine the profits from a corporate tax perspective. It can change the overall costs to the company if not correctly managed.

What is the issue?

The International Tax Framework in the corporate tax area has experienced significant changes in the last few years. Countering tax evasion and avoidance has become a top priority at both EU and international levels due to the consequences of the last financial crisis, and weaknesses and misalignments of the international tax system dating as far back as the 1920s. In short, fast changing business models and structures had, over time, become misaligned with the rules that apply to them.

As a result, the OECD and the G20 crafted the BEPS project. This was launched in 2013 with the OECD's report *Addressing Base Erosion and Profit Shifting*. It targets identified deficiencies in national and international tax rules that leave room for loopholes and mismatches.

The project signals the determination of countries, having recognized the international reach of the issue, to coordinate their actions for the elimination of the deficiencies. Two years after the project was launched, specific recommendations had been issued by the OECD on the appropriate measures at national and international levels. 15 areas of action were identified as priorities. The work proceeds at a fast pace with more and more countries implementing proposed changes.

Two BEPS actions that require closer attention from global mobility perspective are: Action 7: preventing the artificial avoidance of permanent establishment status and Action 13: country by country reporting.

In view of the latest BEPS changes, it is advisable to review intercompany agreements and transfer pricing related policies in place, in order to assess whether they meet the recent BEPS standards and do not raise further risks.

Standard policies for the mobile workforce may no longer be suitable if they do not take into consideration the employees activities, role, levels and the nature or value of the services rendered by this mobile workforce.

The impact of getting the transfer pricing right or wrong is all about compliance and tax efficiency. For example, a tax authority may not allow a sending company to deduct the costs of an assigned worker from its profits. In the receiving location, the company may not be deducting enough costs. As a result, too little or too much profit may be taxed in the two countries. This issue, when it applies to many employees over many years can over time become a big tax issue.

Best practice guidelines

The intercompany secondment usually sees a company temporarily assigning an employee to another company, belonging to the same group, but located in a different jurisdiction. The hosting company would normally, directly or indirectly, benefit from the activities carried out by the employee.

Under current best practice, the company should properly prepare and keep accounting and contractual documentation that clearly shows and describes the activities and related costs of the seconded employee. This can include:

- secondment terms and conditions
- description of functions and activities to be performed by the seconded employee
- details of recharged costs
- criteria to determine recharged costs
- how to split secondment costs between the companies involved.

Often, the costs that are recharged between the entities are the labour/payroll costs. However, entities may agree a mark-up on the costs in order to recognise and compensate for the full service being provided by the seconding employer.

It is always advisable to clearly identify who bears which cost within an intercompany secondment agreement between the two companies (sending and receiving). This is usually separate from the secondment or assignment agreement with the employee.

The company who assigns the secondee remains their employer for the duration of the secondment and, may continue to pay actual salary and wages, administer employee benefits, bonuses, taxes, employment insurance, and social security payments. These costs and expenses will then be reimbursed by the hosting company, who may also bear additional travel expenses, board and lodging, materials and supplies directly provided to the secondee.

The sending and receiving companies can determine how the costs are recharged between the companies. It will be necessary to consider the business goals of the assignment, the mobility policy type, where the short and long term benefits sit and what appropriate mark ups should apply.

It should also be noted that the cross charging to a group company can also lead to changes in compliance. For example, the cross charge may prevent an exemption under a tax treaty (so income taxes are triggered) or it could be a determining factor in whether, or not, payroll is triggered in the receiving country and company.

What action is required?

In view of the BEPS changes, it is advisable to review intercompany agreements and people related transfer pricing related policies and approaches to assess whether they meet the recent BEPS standards and do not raise further risks. As mentioned above, standard policies for a mobile workforce may no longer be suitable.

Additional considerations

Taking into consideration the changes on permanent establishment (PE) thresholds as part of BEPS a mobile workforce might also give rise to hidden PE risks. PE risk is covered in a separate Mobility Monday article. It would be also wise to review what capacity seconded employees keep to negotiate and sign contracts or whether they have an advisory and more consultative role.

BEPS has increased also reporting and transparency. Another relevant consideration for global mobility is country by country reporting, which deals with the reporting of the number of employees on a full-time equivalent basis. How are globally mobile employees dealt with?

Conclusion

In global mobility, transfer pricing concerns itself with the cross charge of costs between group companies in respect of employees.

Recent developments at a global level mean that this area required careful review so that too little or too much tax is not paid, and the arrangements are robust and reasonable on review by a fiscal authority. It's a key area for mobility/HR professionals to work closely with finance and tax experts.

[Filipa Correia Crowe Valente,](#)

Italy

[Pietro Schipani Crowe Valente,](#)

Italy

[Laura Saconne Crowe Valente,](#)

Italy