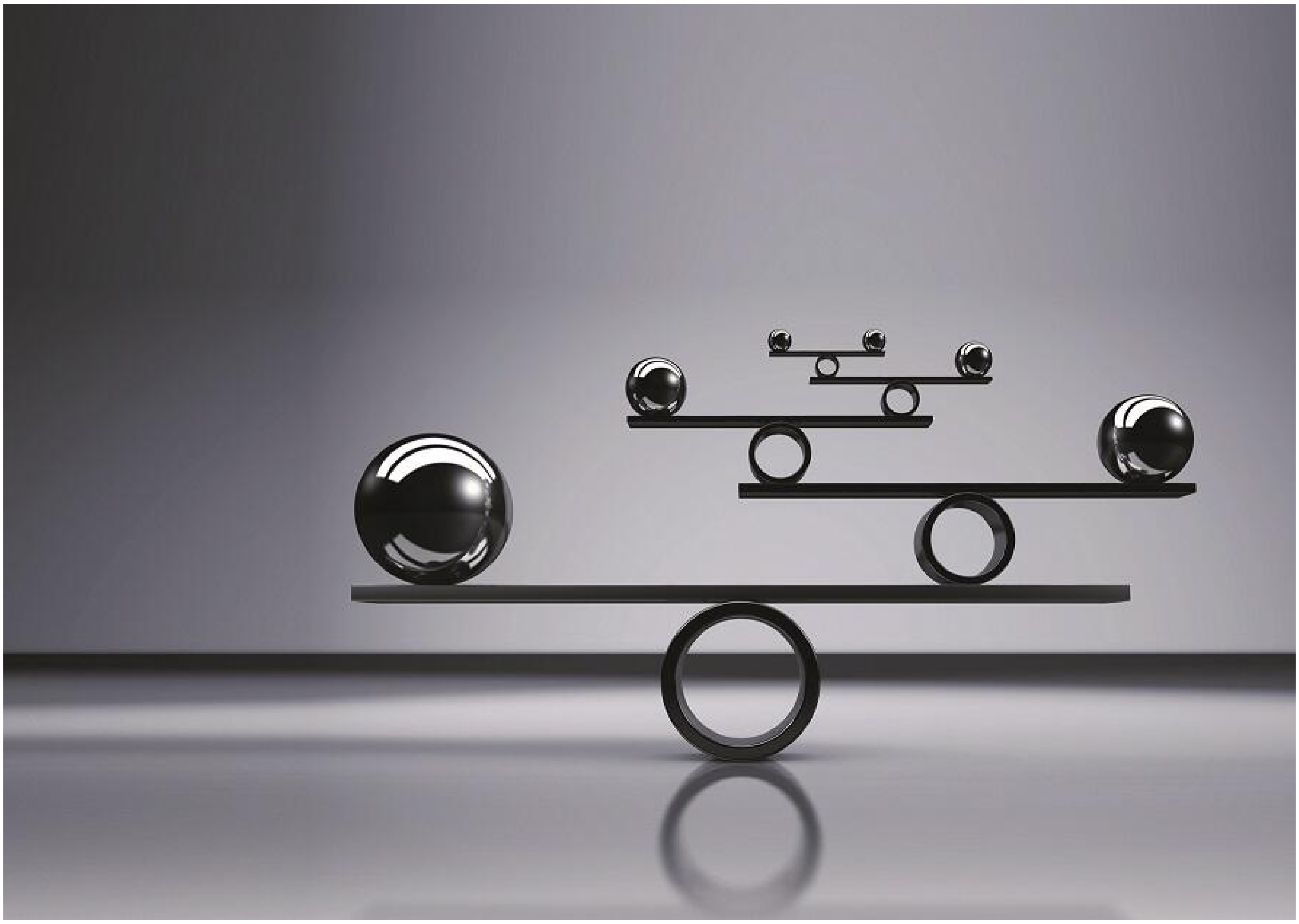
Managing global compliance

Employment Tax | Large Corporate



01 February 2019

Stephanie Symonds-Dye and *Ken Blanchard* consider the challenges of UK companies issuing shares as long-term incentives while adhering to global compliance regulations where they have employees

Many employers incentivise their employees by issuing share awards, such as Stock Options and Restricted Stock Units. Implementing and operating these incentive plans can be complex and often large companies have teams of share specialists for this purpose. However for smaller companies entering new markets these differences can come as a rude shock.

Multitude of taxation approaches

It is fairly evident that income tax rates and regulations vary dramatically around the world. For multinational companies, it is vital that income tax obligations in all operational locations are well understood and this is often achieved by relying on advisers, either local to each jurisdiction or one with a global remit. The complexity starts at the most basic questions, ‘what is tax payable on’?

What is tax payable on?

Many jurisdictions have specific rules to *defining* the tax market value for share awards, e.g. the ‘closing price’, ‘quarter up’ or ‘30-day weighted average’ methods. India requires a Merchant Banker’s valuation to be used for foreign shares although companies are only required to update the value every six months. The method may also change where shares are disposed of as part of the vesting process. HMRC generally allows the use of the disposal price where the company undertakes a bulk sale of shares at the vesting date but only if completed within in two days. If there is a delay in the sale process (e.g. due to limited liquidity in the market) a market valuation must be used.

On a completely different spectrum, some locations (such as Russia, Indonesia and Chile) will base the taxable amount (or at least the amount subject to withholding) on the value of any recharge received by the local entity and claimed as a corporate tax deduction. This requires more consideration around where the cost to the business of the award sits.

How is tax payable?

Most companies will require employees to sell enough shares at the taxable date to fund the withholding tax. This can fall down where the taxable event in the remote location is different to the UK. For stock options that are normally taxed at exercise in the UK, where an employee works in a ‘tax at vest’ location the company must have systems to track the award vesting and collect payment from the employee in order to be compliant in that location even if the employee chooses not to exercise.

Given the employee has neither shares to sell nor cash to fund the taxes at that point, more creative solutions may be required such as triggering an automatic exercise of the relevant awards or the use of employee loan.

Unsurprisingly the use of a loan will often create broader implications for both the corporate and the employee, including tax and accounting implications to name a few.

Employee considerations: personal tax returns

It would be remiss not to note that the success of a corporate’s ability to withhold correctly can have a significant impact on the employee themselves. This is particularly evident if the employee has a personal Tax Return filing obligation and is faced with including stock income which may not have been correctly taxed at the withholding stage. In most cases, this will not relieve the corporate of their withholding obligation but will add more complexity to the Tax Return process and will often leave the employee without the correct payroll documentation (such as an annual statement or P60 equivalent). It can also create unexpected tax liabilities at the Tax Return stage (for example charges under ITEPA section 222).

Movers and shakers

Where a company has operations in multiple countries, chances are it has executives moving between those countries who hold equity awards. So once the company has determined the requirements for their local populations, it is necessary to then look at the cross border cases. These usually make up a small percentage of the participants but have the biggest number of issues:

Not all countries follow the OECD model for ‘sourcing’ employee equity awards for granting double tax relief. This is normally based on workdays between grant and vesting. This leads to planning opportunities but also risks significant double taxation. These cases can be very difficult to resolve even through tax treaty Competent Authority requests as both countries believe they are taxing their fair share of the income. For example:

- Countries with less developed tax systems may simply take an ‘all or nothing’ approach, looking at the person’s residency at the relevant event date.
- Expats going in and out of Singapore often face issues as Singapore will tax all awards in full where they were granted in respect of Singapore employment (including levying an exit tax at departure on unvested awards) but does not tax awards granted prior to arrival in Singapore.

- As mentioned above, a country may ignore the location of work entirely and simply tax based on the relevant corporate recharge.

Even assuming both countries agree on sourcing, the resident country may not permit double tax relief to be claimed at the time the employer is required to withhold the tax and may only allow it via the tax return. In the worst cases (e.g. the employee moves just prior to vesting), it is possible to have a total withholding requirement of more than 100% of the value of the award.

Finally, the apportionment rules may be different between income tax and social security. The Foreign Securities Income rules introduced in FA2014 and FA2015 set out different sourcing methodologies for Income Tax (which looks at periods of tax residence and workdays in the allocation period) and National Insurance (which looks at what periods the employee was subject to NIC). This issue is not unique to the UK and effectively doubles the number of calculations the local payrolls need to undertake.

Summary

The operation and implementation of a share plan for multinationals is complex and companies are not able to apply a one size fits all approach. Each jurisdiction they operate in must be reviewed at all stages of the share lifecycle, from grant to sale, to determine what, if any, obligations arise in that location. Critical to the success of this is local jurisdictional knowledge and regular reviews of key locations to ensure updates in legislation are understood and addressed prior to their implementation.