GLOBAL EXPANSION

An Equus Software Company

A GUIDE TO SHADOW PAYROLL

Everything You Need To Know

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INTRODUCTION

Today's business world has never before been more interconnected, interwoven, and more interdependent on workers and businesses who hail from nearly every corner of the globe. You see, the globalized economy that we know all too well today can only operate when businesses across oceans are in sync. You see, a global business world means that we live within a global economy. When money is spent in one country, it's earned somewhere else. And when a worker is paid in one country, they are often liable to pay taxes on that income. But what happens when a worker is sent to work abroad in a host country? Suppose they're compensated for that work by their company located in their home country – but what about the host country?

This is where things can get a little complicated – but we assure you, by the time you finish reading this eBook, you'll have a wonderful understanding of just what it means to set up a shadow payroll. Remember, international business is a large, vast, and convoluted network of foreign and domestic businesses, vendors, suppliers, partners, customers, consumers, and more. It'll take some dedication, some commitment, and of course, some research to understand it.

In this eBook, we've broken down the concept of a shadow payroll into simple and easy to understand terms. Throughout the chapters that you'll soon read, you'll immerse yourself in a variety of topics to help provide you with a comprehensive understanding of anything and everything related to a shadow payroll. We'll discuss the fundamentals of a shadow payroll, along with the importance of a shadow payroll, how to implement one, the various types of assignments that workers might be given within a shadow payroll and the responsibilities of home and host countries in terms of payroll and taxation responsibilities. Lastly, we'll talk about some common aspects of expatriate compensation plans before finally rounding out the eBook with two final chapters on common shadow payroll terminology and a simple guide to teach you just how to process shadow payroll.

By the time you've finished this eBook, you'll have a greater understanding of the fundamentals of a shadow payroll, in addition to some helpful and useful insight that will aid you as you plan your international business expansion or your international business endeavours. It'll be critical for you to now only know when it is appropriate to set up a shadow payroll but also to know precisely how to set one up from start to finish, ensuring that you're meeting all of your responsibilities every step of the way.

So, if you're ready to build your knowledge of the global business world, then it's time to start reading and dig into the very core of a shadow payroll. Remember, if you plan on doing any work internationally – even if your sending your domestic workers overseas for an assignment, the concept of a shadow payroll might come into play depending on the host country, so having some knowledge of it before you begin your international endeavours would be wise.

With that said, let's get started.

What Is A Shadow Payroll?

Welcome to the first chapter of this eBook where we'll discuss the fundamentals of a shadow payroll. If you've never heard of a shadow payroll before, then this is a great place to begin. Before we actually look at the true definition of a shadow payroll in terms of today's globalized business world, let's break it down and see if we can define the two terms individually.

First, the word, "shadow" often refers to the dark outline that an object will cast on a surface when light is shined on it. Think of it this way – when you stand outside of your office building at around noon, you should begin to see your own shadow cast on the concrete beneath your feet. Whichever direction you move, your shadow will move with you.

Next, the word, "payroll," refers to the money that we use to compensate our employees. Employees who are on your business payroll are part of your business, and you're required to follow local, state, or federal payroll laws, rules, and regulations in order to keep your employees on your payroll.

If we look at the full term, "shadow payroll," one could assume that it refers to a copy or a duplicate payroll, right? In other words, your payroll will have a shadow – an exact copy. Now, this isn't to say that you're paying your payroll twice – instead, it refers to specific international business practices when there is a home country and a host country involved. That sounds complicated, so let's break it down even further.

What Is A Shadow Payroll?

EY.com describes a shadow payroll in the following terms: “Often when an employee goes on a work assignment where the host nation requires that worker to join the local payroll, this triggers the process known as shadow payroll. That is, the employer needs to run parallel payroll processes, one at home to continue paying the employee, and another ‘shadow payroll’ in the host country to meet tax filing obligations.”

So, according to this explanation, a shadow payroll is required when there is a home country business and a host country involved in a worker’s assignment. So, if you’re based in the UK, and then send one of your employees overseas to a foreign country on a month-long assignment, you’ll be required to file the compensation that this particular worker earned during that time period – both in your home country, so the UK, in addition to the host country, which would be wherever you sent that employee.

What’s the purpose of doing this?

Well, there are a number of reasons for why a shadow payroll would be important. First and foremost, if you’re setting up a shadow payroll, then it’s likely for compliance purposes. After all, no business would willingly choose to set up a shadow payroll and assume the risks of doing such unless it were totally necessary.

Going back to EY.com, they say, “Not only is a greater percentage of today’s workforce globally mobile, but host nations are becoming increasingly more demanding regarding who must join their local payrolls. Local tax jurisdictions are recognizing they can significantly reduce their own operating costs by shifting the burden of taxation onto employers.”

And this is exactly what it all boils down to. Many different countries who welcome international businesses and international workers often choose to require businesses in home countries to set up a shadow payroll, so that these international employees are on local payrolls when completing work in a country, ultimately withholding some of that compensation locally.

What Are The Trends?

The trends are quite interesting. Again, if it's any indication, our world is growing increasingly more globalized and interconnected. Workers are often striving towards a remote work position, which allows them to work from home, far away from the offices or headquarters of their employer. This trend, along with the needs, wants, and preferences of a changing workforce is certainly painting a clear picture that shadow payrolls are about to get more and more common all throughout the world.

FreedMaxick has gone into detail on the matter in their blog. In one article, they talked about the growing trend taking place in the United States regarding shadow payroll. Let's take a look at the US as an example: because the US is frequently doing business north of its border with the country of Canada, employers based in the US frequently establish shadow payrolls for their employees during their assignments north of the border.

In FreedMaxick's article, they say, "We see it happening more and more. U.S. companies are sending their employees into foreign (host) countries on temporary but at times lengthy business assignments. Employees are willingly accepting these offers, not realizing the tax exposure risks that these opportunities to present." They go on to suggest that US based employers look to help employees mitigate their tax liabilities through the use of a shadow payroll.

Essentially, the shadow payroll ensures that the employee remains liable for taxes in the US, and that there is also an accurate record of what they would potentially owe if they were being paid in Canada. While an employee is typically not required to pay double taxes – as in the taxes that they'd be required to pay in the US and in Canada, it is important to note that this is still a risk. To prevent this from occurring, many businesses look for tax credits and exclusions, so that their employees won't be required to pay taxes in that host country. There are even tax treaties that can be exploited to prevent this from happening.

Remember – this is just one single example of a US-based company sending a single employee to Canada for an assignment. What about in the EU? After all, countries are much more open there, so what would a shadow payroll look like in the EU?

According to Newrealityblog.com, "if an employee moves their work location to another EU/EEA state or Switzerland and works exclusively from there, companies will generally have to pay the social security contributions in the country concerned. The company has to register in these countries, and in some cases, even has to implement local shadow accounting. There is often the option to transfer the reporting and payment obligation to the employee. In this case, the companies pays the employer and employee contributions to the employee, who then transfers them to the foreign authorities."

Even working from home can get a little complicated. They go on to say, "if an employee temporarily works from home in a foreign country, for example because they are supporting family members and occasionally spend time with the family in another country, it may be possible to remain within the German social security system." However, again, the length and duration of stay in that country will become a factor in determining whether or not the company can work within their German social security obligations.

So, as you can see, although the concept of a shadow payroll might be simple, the scenarios in which it would apply can become quite grey and clouded. It's a complicated concept from end to end, there's no ifs, ands, or buts about it. So with that, what exactly should businesses be looking into when they're preparing to set up a shadow payroll?

What A Business Needs For A Shadow Payroll

When it comes down to it, there are certainly a number of risks that are associated with a shadow payroll, and that's something that we'll talk about shortly. Before we get there, let's talk about some of the musts that employers and businesses need to guarantee when setting up a shadow payroll to avoid any potential risk.

EY.com points to five essentials, and we'll discuss them and dissect them down below:

Stay Up To Date

One of the most important things you can do to handle the necessity of filing a shadow payroll is to ensure that you're always up to date with tax obligations in the countries in which you plan to do business. For instance, if you plan to send an employee overseas, be sure to conduct enough due diligence research in the months and weeks leading up to their departure, so that you're fully aware of yours and your employee's tax obligations in their host country throughout the duration of their assignment.

Develop A Global Policy

If you plan to do business internationally, then you need to have a single, unified organizational global policy that dictates exactly how you do things abroad. This will help to ensure that employees all throughout your various departments and across levels understand when certain measures need to be taken to avoid and mitigate risk – like establishing a shadow payroll.

Know What Matters

Often times, the rules and regulations that govern the requirement of a shadow payroll filing in foreign countries can differ quite a bit. And not only that, but the specifics that dictate whether or not an employee needs to file a shadow payroll throughout their assignment differ as well. For instance, the amount of time, the type of work or services performed, where the employee is staying during their stay, tax treaties, and so much more can come into play – and you need to know it.

Be Alert For Changes To Plans

Remember, no business operating today does things perfectly. Things change frequently – mostly as a response to the dynamic, fast-moving, and ever-changing world that we live in. If the COVID-19 pandemic was any indication, it's clear that things in the international business community can change on a dime – and that might affect your employees overseas. Always consider changes, holdups, delays, and more, so that you can adequately plan for a shadow payroll.

Invest In Technology

Having your payroll staff manage multiple shadow payrolls for multiple overseas employees might not be the smartest and most efficient way to go about. Instead, you can work with technology to automate your shadow payroll calculations in real-time, keeping things fast, neat, and accurate. Investing in the right software applications to help you along the way will save you time, stress, and money alter on when it's time to pay those taxes.

Now, it's important to keep those five points in mind, and we'd like to thank Ey.com for bringing them to our attention. If you follow these points, then you should put yourself in the best possible position to avoid taking on some added risk with your overseas ventures.

We've said it a few times so far, so we'll say it again – a shadow payroll certainly comes with risk, and your goal as a business owner is to mitigate that risk. What are the risks, you ask? Well, let's talk about those before we round out this chapter.

The Risks of A Shadow Payroll

Most of the risk that you'll assume when setting up a shadow payroll will revolve around fines – either from your home country or the host country in which your employees are assigned. For instance, a company could potentially send workers overseas for short-term assignments and fail to report their compensation to the local tax authorities in that host country – this would likely come along with a fine for a failure to report.

Perhaps you sent an employee overseas for a long-term assignment and simply neglected to continue calculating your social security contributions in your home country – that likely result in a hefty fine from your home country.

And of course, there is also the potential that you could potentially overpay your employees' payroll tax withholdings both in your home country and in the host country – and that would be detrimental. After all, the likelihood of you getting back some of that money is close to nonexistent.

Moving On

At this point, you should have a healthy understanding of what a shadow payroll is, and how it works – at least fundamentally. Next, we're going to get a bit more specific into the importance of a shadow payroll. This next chapter should provide you with a bit more insight into when and why you'd want to use a shadow payroll for your international business endeavors.

What Is The Importance of A Shadow Payroll?

So far in this eBook, we've touched upon the reasons for why a business would potentially choose to set up a shadow payroll for their international workforce. However, we haven't exactly underscored the importance of this payroll mechanism just yet. So, in this chapter, we're going to take a long, hard look at the characteristics of a shadow payroll, so that you truly understand just how critical it is for you to set one up for each and every last one of your employees whom you send overseas on short, long, or durational assignments.

There's A Difference Between Expatriates And Home Country Employees On International Assignments

One of the most important aspects of a shadow payroll is that it makes a clear and clean distinction between an expatriate and a home country employee who has been sent on an international assignment overseas into a new host country.

Expatriates, according to an article published on immedis.com, is "an employee who is transferring on a long term assignment from the US to another country," and "is covered by a company-sponsored mobility package." In essence, expatriates are governed by different rules than a home country employee who has been sent on a long-term assignment. Attaining Expat status is a complex legal process that typically revolves around government rules and regulations – for both a home country and a host country. Not to mention, like immedis says, an expatriate is typically covered by some sort of company program or package.

A shadow payroll, on the other hand, is a bit less legal-driven. Instead, it deals more with taxation and finance. However, it's also important to keep in mind that an expatriate would be required to have a shadow payroll, but not every employee who works overseas on an assignment has expatriate status – if that's clear.

In other words, a shadow payroll is often required, regardless of expatriate status or not. That's why it's so important to make sure that you're well aware of the rules and regulations in each host country. While your employee might not have to attain expatriate status, you still might be required – and likely will be required – to establish a shadow payroll.

FOREIGN GOVERNMENTS REALLY ARE PAYING ATTENTION

We've made note a few times throughout this eBook so far that shadow payroll is becoming more and more common as our world becomes more and more interconnected and globalized. You see, host countries have realized the value in tracking payroll for international workers to come to their country's on assignment, so that they could potentially reap the benefits of taxation.

With that said, it's clear that foreign governments are increasingly paying more and more attention to the workers who come from overseas in terms of how long they're staying, how much they're earning, and where they're coming from.

A report by Bloomberg Tax & Accounting says, "employees working in a foreign country for an extended period of time, even if they are not receiving any wages in that country, will eventually trigger certain tax liabilities in that foreign country. The main challenges if the fact that employees often remain on their home country payroll and therefore must continue to pay their home country taxes despite the fact that they are overseas and triggering foreign tax obligations."

The report goes on to say, "Bloomberg Law has documented numerous cases where governments are using increasingly sophisticated and unprecedented methods to track and monitor tax compliance with foreign companies and employees."

As you can see, the evidence is here and the writing is written on the wall to see. If you choose not to file a shadow payroll for your expatriates or your employees working overseas, you will likely assume the risk of a fine of some sort – and that's simply no way to do business.

DOING WORK INTERNATIONALLY DOESN'T HAVE TO BE RISKY

At the end of the day, the most important aspect of shadow payrolls is that they help to mitigate risk – and when you're working internationally, there's always a risk. With that said, if there's any opportunity to reduce some risk in one area, it's always a good idea to take advantage of it. For that very reason, we always advocate for filing a shadow payroll for any and all employees working overseas, even if you're within the time threshold or haven't met all of the requirements within the foreign host country. Remember, it's always wise to account for changes, delays, disruptions, etc., which could potentially be enough to push you over that time threshold or satisfy more requirements – and at that point, if you haven't already established a shadow payroll, it could be too late.

So, the true importance of filing shadow payrolls should be plain and simple for you now. In nearly all cases, it's worth it to file it, because why take on the added risk when it's simply not necessary?

All this talk about the necessity of setting up a shadow payroll, and we haven't even told you how to do it just yet. Well, you could look it up – or you could simply follow the steps that we're about to outline in the next chapter, which is dedicated to the implementation of a shadow payroll for your international employees. If you're ready to learn more about how you can establish a shadow payroll, let's move on to the next chapter.

How To Implement A Shadow Payroll For International Employees

Now that you've learned all about the fundamentals of a shadow payroll, it's time to learn how to actually set one up. In this chapter, we're going to take a look at a hypothetical example to help you fully understand the exact steps that you'd need to take – from the moment you plan an employee's overseas trip, to the final step of calculating their shadow payroll. This process is quite simple at face value, but you might soon find yourself seeking the assistance of an tax or a financial professional to clarify things – and that's okay! After all, as an international business, you're tasked with knowing not only the laws and regulations that govern your host country, but also those of the countries in which you plan to do business.

Also, before we get into this chapter, we want to note that this is specifically a guide for implementing a shadow payroll for international employees – meaning employees whom are already based in other countries. If you're looking for a guide on how to implement a shadow payroll for your employees whom are actually based in your home country, we'll save that for later on in this eBook.

WHAT IS AN INTERNATIONAL EMPLOYEE?

Many businesses that choose to conduct business within the global market often have some employees who are based in other countries. Now, this would be a bit different from a shadow payroll or an expatriate situation. More than likely, those businesses have formally incorporated into those foreign countries, meaning that they're 100% fully and completely liable for taxation, financial obligations, legal compliance, etc. Essentially, those international entities, although in partnership and under ownership of the HQ back in the home country, are considered separate businesses to an extent in the host country.

In this scenario, your employees in that foreign country would be considered home-base employees in that country. You would not be required to establish a shadow payroll, because those employees are already paying taxes in that locale. However, should you choose to send one or some of those employees on an assignment to another country in which you do not own an incorporated branch of your business, your international branch would be required to implement a shadow payroll for each employee overseas.

IMPLEMENTING A SHADOW PAYROLL

Now, implementing a shadow payroll isn't necessarily difficult, but making sure that you've got all of your pieces in the right place is absolutely critical. Without this, you could put yourself at risk of financial obligations or legal issues – which is something that you should make every effort to avoid.

With that said, let's take a look at our simple, 5-step plan to help you implement a shadow payroll for your international workers:

Step 1: Confirm Your Employee's Home Country

Remember, for your international employees, you first need to confirm exactly where they're based. If they're based in your home country, then something's wrong. They should be based in one of your international branches – and if that's the case, then you'll want to use that country as your employee's home country. So, say for instance, your home base and HQ is in the US. However, you've got a secondary branch and a fully incorporated office in the UK. Your UK-based employees are all on the UK branch's payroll. Now, you plan to send one of your UK workers to Switzerland for a 1-year assignment. The home country of that employee should be set to the UK. From here, it'll be up to your UK staff to add that particular employee as a jointer onto their home country payroll. Essentially, that particular employee and your UK branch will be required to remain in compliance both in the UK and in Switzerland throughout your employee's stay there.

Step 2: Process Your UK Payroll With Variable Pay Elements As Usual

Next, you'll want to be sure that you process your UK payroll with all variable pay elements as you typically would. In other words, you'll calculate your taxes, national insurance, and any other important liabilities like retirement, benefits, and more. This is an important step to ensure that you remain compliant in your home country. Even though your employee might not be completing work in your country, you're still liable for them on your payroll.

Step 3: Prepare Your Payroll Reports

Now, depending on how you handle payroll in your company, whether it be with an internal payroll staff, or with an outside payroll company, it'll be absolutely critical that you have all of the right documents in hand, so that they're well aware of your employee's work overseas. Remember, your employee won't be compensated for their work by Switzerland, so it'll be critical that you continue to file their payroll reports to whomever or whichever entity you task with compensating your workforce.

Step 4: Add Your UK Employee To Switzerland's Payroll As A New Starter

This is where things become a bit more critical. Once you've handled your payroll in the UK, it'll be important to add your overseas employee to Switzerland's payroll as a new starter. Under this status, the employee will essentially be placed into Switzerland's payroll system.

In order to ensure that your employee isn't taxed twice on their earnings, it'll be up to your UK team or payroll provider to reduce any taxable payments to zero through the use of a net deduction on payroll. Any and all criteria including salary, commissions, and potential bonuses must be recorded on both the home country payroll and the hot country payroll. Not to mention, you need to also apply for any potential net of foreign tax schemes to grant the removal of the host country's tax requirements and any other contributions that your employee might be liable for.

Step 5: Tax Equalization

Last, but not least, you'll need to engage in a process called tax equalization. More than likely, your application for a net of foreign tax scheme will be accepted, and you won't have to worry about hypothetical tax. Tax equalization essentially allows the home country to take care of the taxes that the employee would technically be required to pay back to the host country for earning while working in that country.

The purpose of this fifth and final step is to ensure that you've covered your employee's tax obligations while overseas. Essentially, they should only see tax withholdings from their home country – not from Switzerland.

WHAT ABOUT THE LENGTH OF AN ASSIGNMENT? WHEN DOES THAT COME INTO PLAY?

This is a great question – and it's something that we'll talk about in the next chapter. So far, we've mentioned a few times that the length of time one of your employees spends in another country for work-related purposes might dictate their potential tax liabilities for that host country. This means that you'll need to take into consideration the duration of time that you envision your employee spending in that host country, so that you can be prepared to handle the tax obligations on their behalf.

So, if you're ready to learn all about the length of assignments, let's move into the next chapter.

Types of Shadow Payroll Assignments: Short, Long, & Permanent

In this chapter, we're going to provide you with a quick rundown regarding the different types of assignments that would typically require an employer to set up a shadow payroll for an employee working overseas. So far in this eBook, you've learned all about the fundamentals of a shadow payroll in terms of what it is, its importance, and how to implement one for your international employees who are already working overseas. Remember, we've mentioned it a few times so far, but it's important to know the rules set forth by each host country in which you plan to send employees. One host country might require taxation after a shorter period of time than another, and it'll be up to you to have that knowledge already tucked away in your plans, so that you can mitigate and potential financial risk and liability.

SHORT BUSINESS TRIPS

The occasional business trip isn't exactly something that's unheard of in a world that is so interconnected as the one that we know and live in today. In fact, it's extremely common for businesses to send some of their team members overseas for international trips – whether it be for a conference, a meeting, a consultation, a sales pitch, a contract negotiation, etc. Here, the sky is the limit. For most businesses, this is totally normal and common place, and these short business trips certainly aren't long enough to warrant even the mere consideration of having to pay the host country's taxes and insurance liabilities.

Short business trips are almost always covered by some sort of tax treaty because the trips are almost never going to be longer than six months. In fact, as long as this "short" business trip remains shorter than 6 months, you'll likely never have to worry about foreign taxes. In these instances, you'll simply withhold taxes as normal and your employee will remain on their home country's programs.

SHORT-TERM ASSIGNMENTS

Short-term assignments are where things begin to change. You see, these assignments are much longer than just a short business trip that might last 2 to 4 weeks, or 6 months at the most. Short-term assignments typically range anywhere from 6 months to 1 full year. During this period, you won't be able to rely on tax treaties to keep your employee on your home country payroll, and that country alone. Instead, you'll likely be required to place that employee on the payroll of your new host country.

Depending on the country, the length of the assignment, and a range of additional factors, some or all of that employee's compensation for the short-term assignment might be taxable in that host country – and that's something that you'll need to determine, and will likely want to determine sooner rather than later. Although this employee will still remain on the social security program of their home country, you will certainly be required to file shadow payroll in this scenario. This will help to ensure that you're keeping track of how much money your employee might be liable for in the host country. From there, you'll have to use various mechanisms at your disposal, so that your employee does not have to pay taxes twice.

LONG-TERM ASSIGNMENTS

The general rule around the world is that if an employee is working overseas for more than 183 days, it would be considered a long-term assignment. Under a long-term assignment, you will absolutely be required to file a shadow payroll, in which case, you would want to follow either the guidelines in the previous chapter, or the guidelines that we will get to in the last chapter of this eBook.

PERMANENT ASSIGNMENTS

In the event that you've set an employee up on a permanent assignment in a foreign country, you'd most certainly be required to file a shadow payroll. However, this might not even be the best option. You see, there are a number of routes that you could take when it comes to permanent assignments.

Essentially, a worker who is permanently assigned to work overseas, away from the home country of their employer, would almost certainly be responsible for paying their fair share of taxes in the host country in which they work. To save yourself the trouble, you might want to consider formally incorporating in this region, so as to protect yourself and your employee from falling victim to overpaying on taxes and other liabilities.

In another scenario, it might even be more beneficial to simply work with a global PEO – or a professional employer organization. If you're not already familiar with a PEO, you should check out some of our additional eBooks, publications, and articles to learn more.

In a nutshell, a global PEO is a company whom you'd partner with and would grant them the ability to hire employees on your behalf. Essentially, they'd become your Employer of Record. They'd be able to hire employees for your business overseas in any country in which you'd like to tap into. From there, those employees would be under your leadership – however, they'd be under the PEO's payroll, which would eliminate any and all payroll and tax responsibility, along with benefits, compliance issues, and more.

For permanent assignments, we believe that working with a PEO is always the best way to go. It simply makes the most sense because you'll never have to worry about handling all of the complex taxation issues that often arise with shadow payrolls. In addition, you wouldn't have to go through the time consuming and expensive process of incorporating. Instead, you can simply go about your business and begin exploring new markets overseas with a dedicated workforce hired, vetted, trained, and paid by your partnering PEO.

NAVIGATING PAYROLL RESPONSIBILITIES

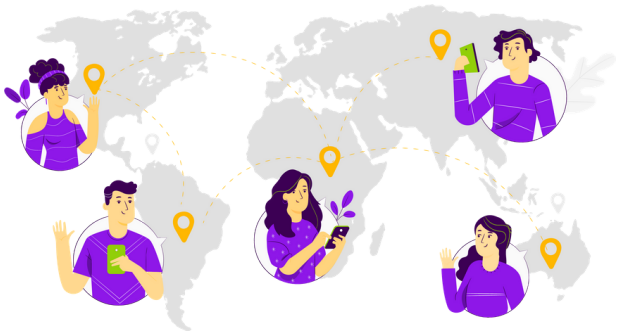
Now that you've learned more about the different types of assignments that might require you to file a shadow payroll, it's time to take a look at the actual payroll responsibilities that come along with a shadow payroll – from both the home country and the host country.

Let's take a look at this in the next chapter.

Host Country or Home Country Payroll Responsibilities

At this point, you should be well aware that there are two major players who have some skin in the game when it comes to shadow payrolls – typically, these are the host country and the home country. Now, whether or not you're part of the home country or the host country, you are going to have a number of important payroll responsibilities, all of which will dictate whether or not you're in full compliance with your national laws and tax obligations.

We're going to take a few moments in this chapter to clearly define and outline the differences between host countries and home countries, so that you fully understand exactly how the process of filing a shadow payroll works – at least in terms of responsibilities.



A HOME COUNTRY

According to iipay.com, "the home country is the country in which the net pay is paid to the employee." So, more than likely, this would be the country in which your business is based; where your employee works the majority of the time, and where your employee lives. If your business is based in the US, then your employee is based in the US as well. In this scenario, your employee would be enrolled in US payroll, would be responsible for US tax obligations, and would be part of retirement and savings benefits like 401(k), social security, Medicare and Medicaid, and more.

As the home country, you're responsible for sending that employee a paycheck. On the paystub that comes along with each paycheck, your employee would be able to track how much federal, state, and local taxes have been withheld. In addition, they'll be able to clearly see their contributions made to social security, unemployment, healthcare, insurance, etc.

Businesses based in a home country that wish to send an employee overseas for international work for a period greater than 6 months would likely be required to file a shadow payroll. We've talked about this quite a bit throughout this eBook so far, so you should already know this. As the home country business, you'll be required to complete all of the steps listed in the chapter on implementing a shadow payroll.

A HOST COUNTRY

On the other hand, iipay.com says, "the host country is the country in which the employee receives no payment. It is important to note here, however, that the home country is not automatically the country from which the employee originates."

This is where things get a little bit confusing – so stick with us as we move through this next example. Now, remember a few chapters back where we provided you with a guide to help you understand how you can file a shadow payroll for your employees who are already working outside of their home country. This is where iipay's definition of a host country comes into play.

You can't automatically assume that just because your employee originated from your home country, it means that this is still their home country. So, suppose that your business is based in the US. You have an employee whom you frequently send overseas. You've sent them on a long-term assignment to Norway, where they stayed and worked for more than 183 days. Again, going back to the previous chapter on assignments, because this employee remained working in Norway on assignment for more than 183 days, you were required to file a shadow payroll.

Now, suppose your employee has completed their work in Norway and they spent a total of 267 days in the country. Instead of bringing them back home to the US, you're sending them on another long-term assignment, where you'll likely be required to file another shadow payroll. This time, they're heading over to Germany, where they'll stay for another 183 days – at least.

In this scenario, the US would no longer be considered the home country of this employee. Instead, Norway would become the home country, since that employee worked their for greater than 183 days (remember, 267 days total). At this point, your employee would be liable for paying taxes in Norway, not in the US. They'd likely have to file a shadow payroll in the US, Norway, and Germany simultaneously, ultimately complicating the financial and legal liabilities that come along with working in each country.

WHAT HAPPENS NEXT?

Let's suggest that you don't even plan on sending your employee on another assignment. Suppose your employee remains in Norway for more than 183 days. At that point, the home and host countries would switch. Your employee's home country would be Norway, and your home base would become the host country for that particular employee.

It can begin to get confusing here, which is why it's so important to be very well aware of the duration of time your employees will spend overseas. In addition, it is absolutely vital that you're educated and up to date on all of the requirements of your host country.

For multinational businesses, you're likely to face a number of challenges with your shadow payroll processes, simply because the process just isn't as clear cut and dry as it sounds on paper. Sure, we make things at least sound digestible in this eBook, but the fact of the matter is that any international business endeavor will come with a great deal of legal hurdles, bureaucracy, financial challenges, and more.

Some common challenges that businesses face revolve around determining just how much money needs to be calculated for your overseas employees. From there, how much money do you need to report to the host country and to your home country? And what about remittances? What needs to be accounted for there?

Calculations come into play too, and those can get dicey as well. How will you calculate your payments and your tax liabilities? Will your internal payroll team handle the job? Will you choose to go with an outside payroll company to lend a hand? And lastly, when should you begin the process? Is there a clear-cut answer for when you should begin calculating? When do you file reports?

You see, these are all valid questions, and their certainly questions that will come up throughout this process. It'll all depend on the rules and regulations set forth by your home country and host country, and that's simply something that you should be aware of beforehand, so that you can prepare well in advance to meet some of these challenges head on.

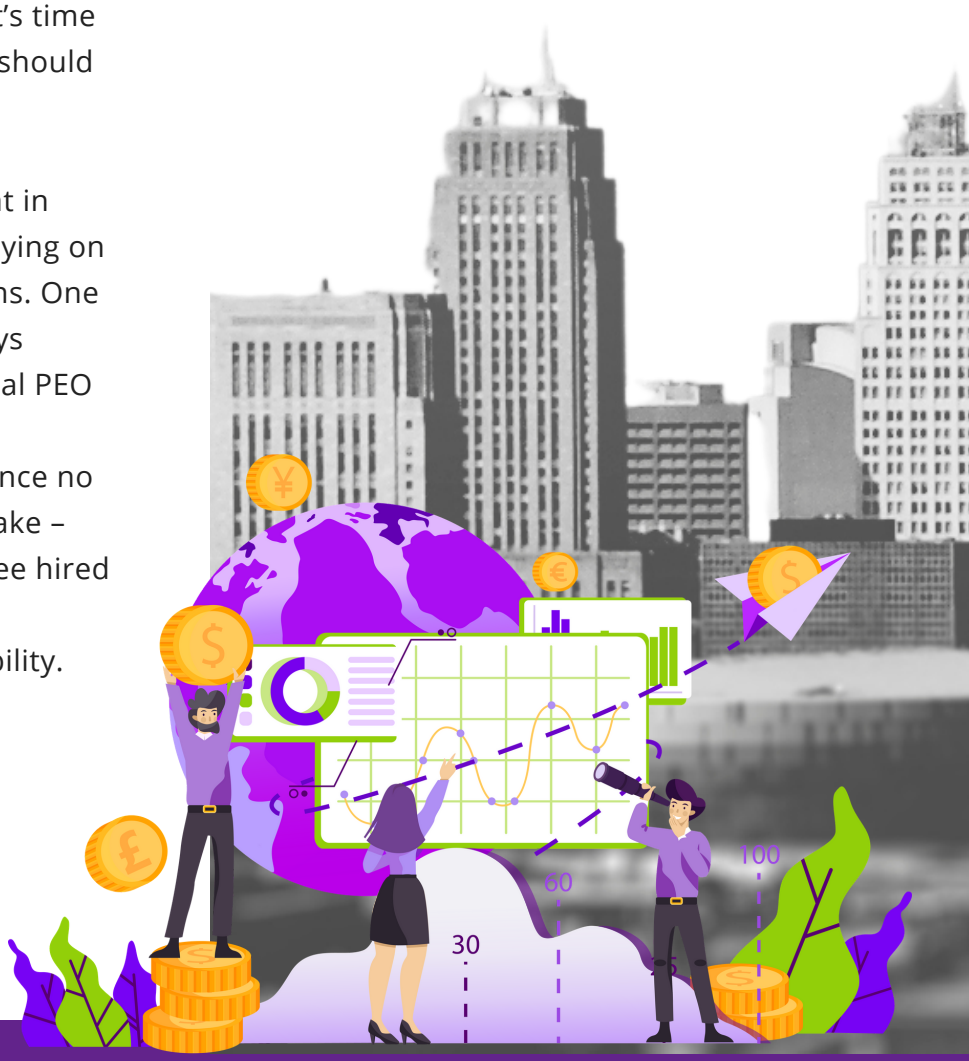
THE WORLD IS GROWING INCREASINGLY MOBILE

The purpose of this chapter is not to stress you out or to create feelings of overwhelm – it's simply to emphasize just how quickly this world is growing increasingly mobile. You see, businesses – specifically, multinational businesses – are moving their workers around faster than ever before. They're merging with other companies, acquiring new companies, shifting assets, opening new branches, expanding in new markets, and doing it all at the speed of sound. Most of them are moving so fast, that they don't even have the time to notify their HR departments or payroll departments of their intentions, which could potentially put them behind the 8 ball when it's time to determine whether or not they should have filed a shadow payroll.

You see, nothing is more important in today's fast-moving world than staying on top of your international operations. One of the easy solutions that we always recommend is working with a global PEO to ensure that your international workforce is always in full compliance no matter what moves you plan to make – after all, any international employee hired by your global PEO on your behalf wouldn't exactly by your responsibility.

But if partnering with a global PEO simply isn't part of your agenda moving forward, then it's absolutely critical that you follow some industry best practices to ensure that when it comes time to file a shadow payroll, you do it in a way that minimizes risk and ensures that all parties involved are able to continue working, paying, receiving, and resolving at all costs.

In the next chapter, we're going to introduce some critical best practices that should help you calculate and file shadow payrolls with a bit more ease. It'll be important to embrace these best practices moving forward, especially if you plan on doing more work internationally in the near future.



Best Practices

Multinational organizations already have it difficult – after all, performing on the massive global stage takes some guts, especially in today's fast moving global marketplace. To make matters even more difficult, sending an employee on an international assignment isn't as easy as picking a destination, giving them their objective, and sending them off with a Business Class airline ticket. Instead, each assignment will come with tons of due diligence research into the financial obligations that businesses are required to fulfill in regard to the home country and the host country.

We've covered a lot throughout this eBook so far, and with just a few more topics left to talk about, we figured now would be a good time to provide you with some reassurance. We know that shadow payrolls can be quite complicated, so we wanted to provide you with some clear, easy to understand best practices that can give you the confidence you need to navigate these tricky financial mechanisms with a bit more ease. These best practices are brought to you by payslip.com.

STRONG COMMUNICATIONS ARE KEY

In any business venture, regardless if it's domestic or international, communication is always key. After all, business leaders pride themselves on clear and transparent communication; team members strive for open communication; employees look to provide clear communication for customers and clients – you see where this is going.

At every stage in the business world, strong communication is key. So, in the highly convoluted and complex nature of shadow payrolls, establishing strong communication between the home country and host country is absolutely critical. In other words, find out what you need to know to ensure a swift and seamless experience for your business and your international employees.

DON'T SHY AWAY FROM TECHNOLOGIES

At the end of the day, we live in a tech driven world. With that said, it's about time that any and every business planning on doing work internationally invest in the right technologies to make their lives – and those of their international employees – easier and stress-free. For instance, there are tons of software applications out there that can help to automate some aspects of shadow payrolls. There are also digital reporting tools that make it easier to do calculations and send your reports to home country and host country organizations. Staying on top of your duties as a multinational business begins with embracing technologies that make it easier to do your job.

UPDATE YOUR PAYROLLS

We've talked about it a few times throughout this eBook, but one of the biggest pieces of advice we can give you is to be sure that you're regularly updating your payrolls, making sure that all of your employees are up to date on compensation and benefits. Not to mention, update your payrolls to reflect any changes in domestic or international tax law. This will help to ensure that you don't run into any unexpected liability issues when it comes time to close out your employee's international assignment.

VERIFY YOUR DATA

Throughout your shadow payroll process, you'll likely see an influx of data – or at least you should. You see, you'll be using this data to do your calculations later on when it's time to determine how much tax your business and your employee will be liable for in their host country. It's always critical that you review your data regularly, double checking and even triple checking for discrepancies.

From there, always be sure to verify that all data is complete and captured properly. A great way to do this is to automate your data processes with software applications. If not, entrust your best data analysts to keep things current and accurate.

STAY UP TO DATE WITH YOUR HOME & HOST COUNTRY'S PAYROLL & TAX PROGRAMS

Remember, tax code and payroll programs frequently change over time, which is why it's all the more critical that you're up to date with your home and host country's payroll and tax programs each and every year. This is something that you can do annually, because that's typically when you'd see a change.

We recommend being well aware of planned changes before they go into effect. This way, you can plan ahead and ensure that your team is prepared to embrace whatever changes might be coming and factor them into your shadow payroll.

DETERMINE WHERE EXPATRIATE TAXES ARE REQUIRED

It's also a good idea to determine exactly where you'll be required to pay expatriate taxes. This will often come into play with a number of countries in which you plan to send your workers to for short and long-term assignments. In these cases, we recommend building a taxability matrix for each of these countries, so that you can plan well in advance just how much money you'll be liable for in regard to expatriate taxes.

AUTOMATION IS YOUR FRIEND

Last, but certainly not least – we touched upon this in the previous best practice regarding embracing technology. It's absolutely critical to remember that automation is your friend. Today's world is an automated world, so it would seem counter-productive to avoid using automation to simplify your processes. You could potentially even automate the entire process that we've been discussing throughout this eBook, making your process much more seamless and likely, much more accurate. After all, automation allows you to reduce the likelihood of human error, and it'll make for fast and easy reporting – virtually in real-time.

WHAT ABOUT REPORTING?

As you can see through our list of best practices, we've mentioned the words "reporting" and "requirements" quite a bit. Now, let's actually get into what your role is in terms of reporting and complying with those requirements. Let's move into the next chapter.

Expatriate Payroll Reporting & Taxation Requirements

So, you've got at least one employee currently stationed somewhere overseas in a foreign country on a long-term assignment exceeding 6 months. At this point, you've likely already begun to file a shadow payroll, and you've been communicating with your home country and host country to determine your payroll reporting and taxation requirements, right?

Obviously, this is a hypothetical situation, but it's one that you'll likely be involved in soon once you get your international business plans off the ground. Now, as a multinational company, you'll be required to report your payroll data for any expatriates that you have working overseas to both your home country and your host country. In addition to that, you'll be liable for taxes in both countries. However, there are typically ways to avoid paying those taxes in the foreign host country – we've mentioned all of those earlier.

REPORTING

When it comes to reporting your payroll to both your home country and host country, your process will and should look something like the list that we've compiled below with information from relocatemagazine.com:

"When the home or host payroll delivers net pay to the assignee, details of that payment should be sent to the shadow country to record in their next payroll as imputed income. The process looks like this:

1. *Paying country delivers and selects which compensation items require recording in the shadow country.*
2. *Convert Compensation items to the shadow currency and forward report to shadow payroll department.*
3. *Shadow country records compensation items in the next available payroll cycle and calculates local tax due.*
4. *Shadow country submits calculated tax to the shadow country's local tax jurisdiction on employee's behalf."*

As you can see, the reporting process is fairly straight forward, just as long as you're following any and all guidelines that you've been given by your home country and host country. As long as you're filing these reports with all parties involved, you should be fine to continue international work.

TAXATION

As we've discussed numerous times throughout this eBook, taxation can get complicated because it is entirely dependent on a variety of factors. For instance, short business trips would fall under a tax treaty, which would absolve an employer and employee from paying any taxes to a host country just as long as the trip is less than 6 months long.

Once the trip becomes longer than 6 months and falls under the category of a short-term assignment, the employer and employee will be required to establish a shadow payroll in which they might be liable for taxes in the host country.

Should the trip become a long-term assignment and exceed 183 days, the employee's home country would switch and become their former host country. At that point, they would be required to pay local and jurisdictional taxes in the foreign country, since they have remained under that country's payroll for a period of greater than 6 months.

IT'S TIME TO GAIN YOUR FOOTING

As we approach the final two chapters of this eBook, it's about time that you gain your footing. We've discussed most – if not all – of the technical aspects of shadow payrolls, and now it's time to make sure that you fully understand all of the terminology that gets used when dealing with them in real life.

In the next chapter, we're going to talk about some of the most commonly used terminology when it comes to shadow payrolls.

Most Commonly Used Shadow Payroll Terminology

Now it's time to recap just about everything that we've talked about in this eBook thus far. However, we won't necessarily dive into the nitty gritty of every last topic. Instead, we're going to take a look at some of the most commonly used shadow payroll terminology that you'll likely see and hear once you begin your international endeavors. Let's take a look down below to make sure that we're on the same page moving forward.

SHADOW PAYROLL

Let's go back to our first chapter for a simple definition:

EY.com describes a shadow payroll in the following terms: "Often when an employee goes on a work assignment where the host nation requires that worker to join the local payroll, this triggers the process known as shadow payroll. That is, the employer needs to run parallel payroll processes, one at home to continue paying the employee, and another 'shadow payroll' in the host country to meet the employer and employee tax filing obligations."

EXPATRIATE

Let's go back to the second chapter for a simple definition:

Expatriates, according to an article published on immedis.com, is "an employee who is transferring on a long term assignment from the US to another country," and "is covered by a company-sponsored mobility package." In essence, expatriates are governed by different rules than a home country employee who has been sent on a long-term assignment.

HOME COUNTRY

Let's go back to our chapter on home countries and host countries for this one:

According to iipay.com, "the home country is the country in which the net pay is paid to the employee." So, more than likely, this would be the country in which your business is based; where your employee works the majority of the time, and where your employee lives.

HOST COUNTRY

Let's go back to our chapter on home countries and host countries for this one:

iipay.com says, "the host country is the country in which the employee receives no payment. It is important to note here, however, that the home country is not automatically the country from which the employee originates."

However, for this one, it's important to remember that the home country will eventually switch to whichever country the employee has been based in for a period longer than 183 days. A home country doesn't exactly have to be where your company HQ is, even if that's where you sent them from. It'll all depend on their assignments.

TAXATION

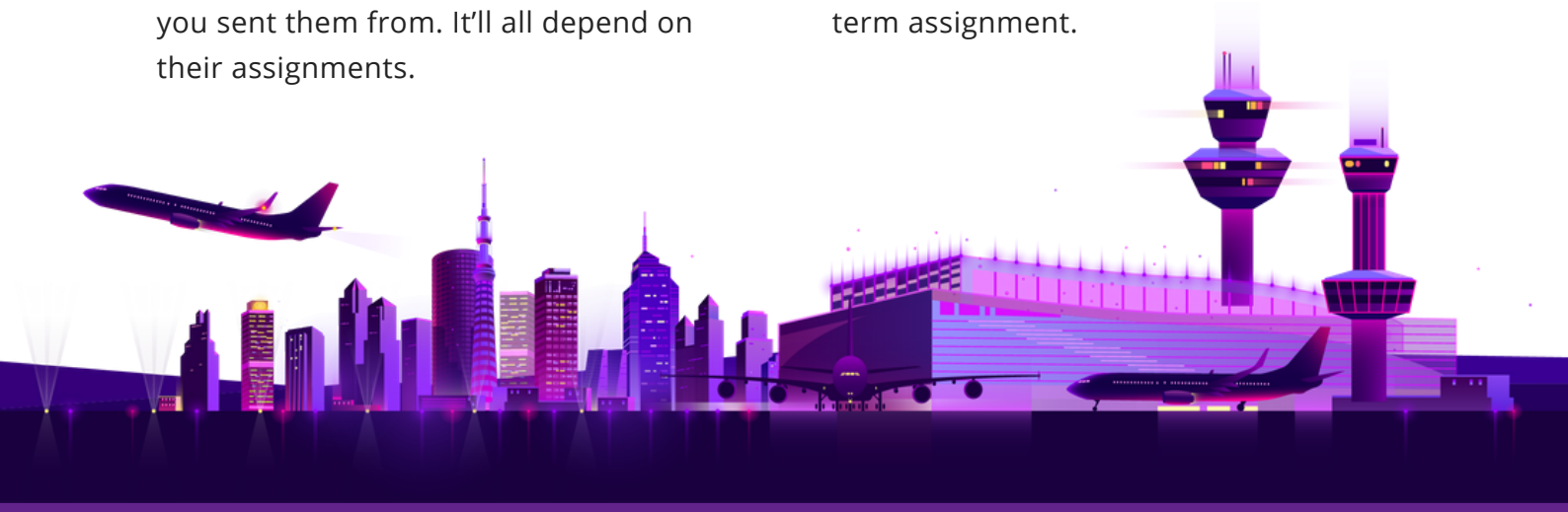
Taxation refers to the money that an employer and employee would be required to pay to a home country or a host country depending on a range of factors.

REPORTING

Reporting refers to the process by which an employer would submit their recorded earnings for a particular employee considered an expatriate working overseas.

LET'S ROUND OUT OUR DISCUSSION

Now that you're aware of some of the most commonly used shadow payroll terms, let's move into the last and final chapter on this subject. You'll recognize it from earlier because it's roughly the same! Previously, we provided you with some simple steps for how to implement a shadow payroll for an international employee, now we'll tell you how to implement one for one of your home country employees whom you're planning to send overseas for a short-term or long-term assignment.



How To Process Shadow Payroll

Here we are – the final chapter of our eBook. At this point, you're likely already familiar with the process of filing a shadow payroll for an international employee. With that said, this final chapter should come easy for you! Let's briefly outline a few necessary steps that you should take to process shadow payroll for a home country employee whom you plan to send on a short-term or long-term assignment overseas.

Step 1: Confirm Your Employee's Home Country

For step 1, confirming your employee's home country should be simple – it's whatever country your business is based in. However, remember, there could be some exceptions to this rule. For instance, if your employee has already been on an assignment in a foreign country for longer than 183 days, the country in which your business is based will no longer be their home country. Instead, it'll be the country that they've been in for their previous assignment. You should remember this from our earlier discussions.

Step 2: Process Your Payroll With Variable Pay Elements As Usual

Let's assume that we're operating under the assumption that your employee is based in your home country – i.e., where your business is incorporated. In this scenario, you can move forward with processing the payroll for that particular employee as per usual, with all variable pay elements considered – meaning benefits, social security, insurance, tax withholdings, etc.

Step 3: Prepare Your Payroll Reports

Remember, reporting your payroll is critical because you'll need to report it to both your home country and your host country. We've mentioned a few times throughout this eBook that it's always a good idea to hire a global payroll company to handle your reporting processes for you to ensure that everything is in compliance with your home and host country, or you could use automated software to do the same thing as well. Whichever route you choose to go, just be sure that your reporting is done accurately and regularly.

Step 4: Add Your Employee To The Host Country's Payroll As A New Starter

This is where you'll want to notify the host country that you've added your employee to their payroll as a new starter. Here, your host country will be able to track and monitor your employee's earnings. In addition, they'll be able to calculate any potential tax liabilities that you and your employee should be required to pay – you know why should is in italics already.

Step 5: Tax Equalization

From our chapter on setting up a shadow payroll for an international employee, we said, "last, but not least, you'll need to engage in a process called tax equalization. More than likely, your application for a net of foreign tax scheme will be accepted, and you won't have to worry about hypothetical tax. Tax equalization essentially allows the home country to take care of the taxes that the employee would technically be required to pay back to the host country for earning while working in that country."

Here, you'll ultimately ensure that your employee does not overpay taxes for both countries.

You're Ready To Process Your Own Shadow Payroll

And with that, you're ready to process your very own shadow payroll!

Well done! You're well-prepared, and you're full of knowledge, so that when it comes time to send your employees overseas, you know just what to expect out of the process.

CONCLUSION

Congratulations! You've reached the end of this eBook – and it's certainly been an informative ride, hasn't it? We're glad that you've chosen to take the time to research shadow payrolls, and we hope that this eBook has provided you with useful insight and information related to the highly complex and challenging mechanism to navigate.

Remember, our world moves fast, and the businesses in it require global partnerships in order to keep the wheels of the economy turning. One of the most important tools that businesses use to send their workers overseas are shadow payrolls, and now your business can utilize this tool to ensure that you're meeting any and all of your tax obligations both domestically and internationally.

Thanks for reading! Don't forget to contact us directly if you have any questions related to shadow payrolls or the materials provided in this eBook. We'd be happy to help and ensure that you have everything you need to make informed business decisions.

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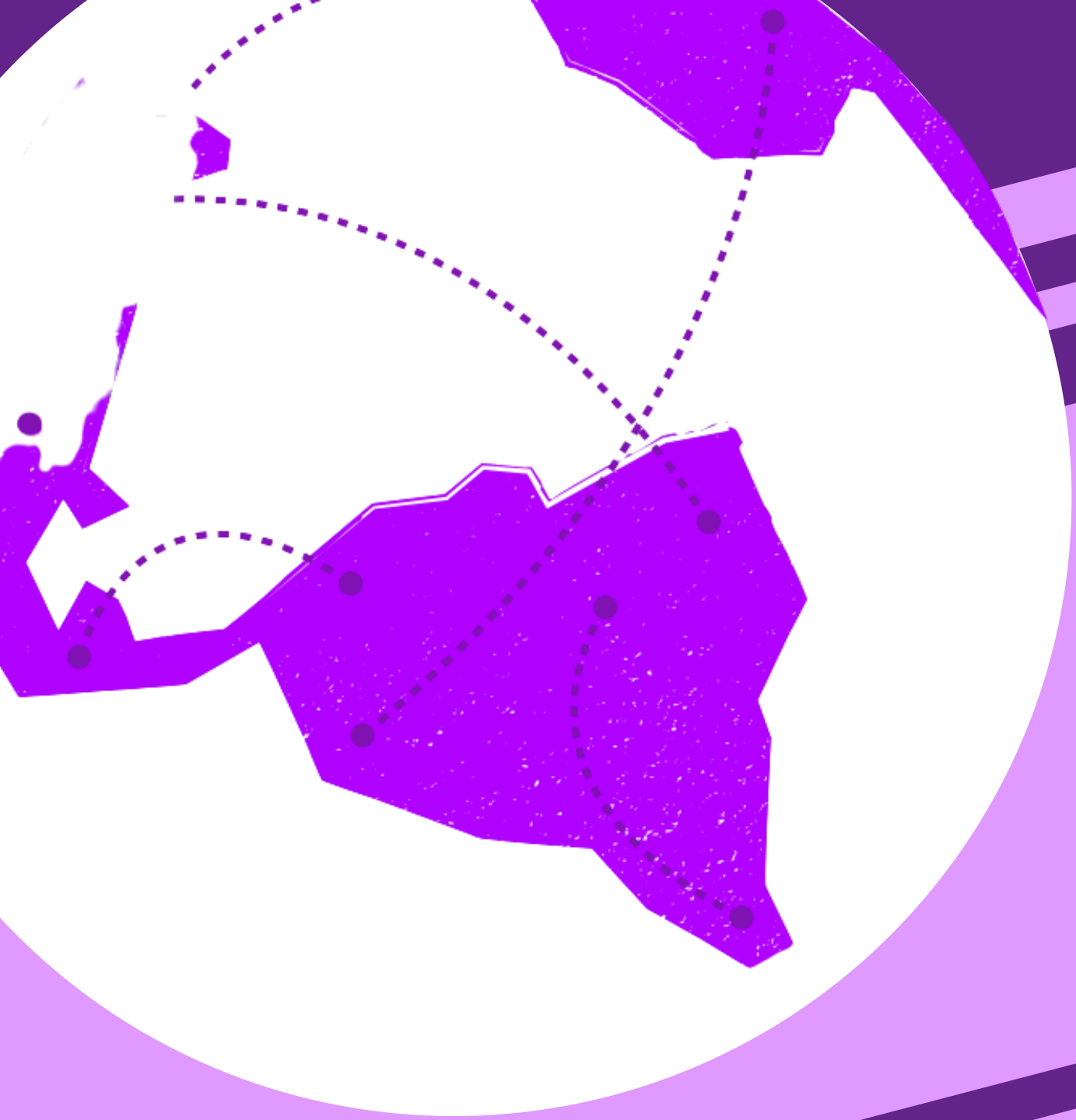

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