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Going global? Top 5 labor and employment issues when expanding outside the US

You are off the ground and running in the US. It's now time to turn your attention to hiring overseas. For many companies, the road to a global workforce can throw up various speed bumps. The key to success (and not losing crucial candidates due to delays) is planning ahead. With the right preparation, onboarding globally can be navigated more smoothly. Here are five key labor and employment issues for growing businesses to consider before going global:

Corporate, tax and doing business considerations

The discussion about how to properly set up your business in a foreign jurisdiction starts with corporate and tax considerations. As a priority, determine your local corporate structure. Many factors, including whether it is permissible to engage employees locally, will depend on it. Some jurisdictions may allow foreign entities to hire employees without a local corporate presence (typically assuming proper payroll withholdings and compliance with local employment laws). However, others don't. For instance, Brazil, China and Russia all require a corporate presence as a prerequisite to enrolling an employee in their mandatory social security systems.

In addition, many countries have "doing business" laws that require a company that is engaged in business in the jurisdiction to obtain a business license or formally set up a corporate presence (such as a subsidiary, branch or representative office). Just as a foreign company that engages in activities in California should obtain a business license, some other countries also take the position that engagement of an employee is something that is akin to doing business and requires proper registration.

Similarly, engaging an employee where the company does not have a corporate presence may create a permanent establishment or taxable presence. Many foreign jurisdictions are increasingly eager to identify tax revenue sources. The most obvious fix is to set up a local corporate presence and ensure proper tax returns are filed. If not possible, while not perfect, the arrangement can be tailored as far as possible to mitigate exposure. Engaging individuals in sales roles typically creates a higher risk in that regard than engaging non-sales individuals, both because salespeople may actually create revenue in the jurisdiction at issue and because they may have authority to make binding sales offers on behalf of a foreign entity.

All that said, as you explore business opportunities in a new jurisdiction, it is not uncommon to skip the legal entity set-up and work on an interim arrangement to get somebody on the ground quickly. Some companies set up a holding company under their ultimate US parent to at least serve as a buffer to some of the liability. While not ideal, as long as they are carefully monitored, such interim solutions are a fairly common way to enter a new market. The threshold issue is how to classify your first hire.

Hiring options

Next up, you need to decide if you will expand by hiring employees or if you will explore other engagement options. As in the US, it is important to determine how to classify the individual and the engagement. Getting this right from the outset is crucial or employment liabilities can be significant.

Employees

Like in the US, most foreign jurisdictions define an employee as an individual working under the direction and control of the employer, in exchange for compensation. If you are a startup, be very cautious when engaging individuals without compensation or for equity only, since many jurisdictions have minimum wage and overtime requirements. See our articles on paying founders and interns. As mentioned above, not every jurisdiction requires a local entity set up to lawfully engage an employee. Most of Europe, for instance, permits the US parent or another non-local company to engage a local hire directly. In that scenario, all you need to do is to obtain a payroll ID, set up payroll, and then comply with all applicable labor and employment laws, thereby avoiding the hassle of setting up a corporate presence before you can lawfully bring an employee on board. However, in some cases, there may be practical reasons why a company may not be able to form a local entity and in those countries where having a local presence is a prerequisite to hire employees alternative routes will need to be considered. Engagement options vary depending on the location, but typically the following are the most common:

Independent contractor

As in the US, this often carries potential misclassification risks. In most jurisdictions courts will look at the actual nature of the working relationship, focusing on direction and control. As in the US, liabilities for misclassification can be significant including liabilities for failure to withhold taxes and social charges, the need to grant past and future employment rights, as well as criminal liabilities in a few jurisdictions. See our article on classifying employees. If an individual is misclassified in the US, that individual is likely misclassified globally as well. There may also be sales agent exposure depending on the country and activities performed by the individual, so it is important to assess that risk. For example, in the EU and some of Latin America local sales agent laws may impose termination notice and indemnification rights to such individuals.

Third-party agency/ PEO employees

If an individual is misclassified, engagement through an agency or professional employer organization can provide some relief, since the agency may be properly compensating that individual. That said, such manpower/outsourcing arrangements may be subject to limitations under local laws to prevent abuse (for example, fixed term time limits, restrictions on controlling the individual providing services, local registration, and in the EU, equal pay rights), so it is important to ensure this meets a company's business needs and is carefully managed.

Expatriate employees: Assigning an individual from the US appears to be an easy solution, but often creates pitfalls. For example, a business visa may not be appropriate if an individuals is going to work in a foreign jurisdiction full time, and, without a local sponsor a work permit is usually hard to get. Most tax treaties require payment of local taxes after 183 days or more in the foreign country, in those cases both the employer and employee may be subject to local withholding liabilities. Also some jurisdictions will deem that local employment laws apply to foreign individuals regularly performing services in the jurisdiction.

Payroll and benefits

Once the structure and type of hire has been determined, you will need to consider the payroll processes and costs, including tax and social charges. In virtually all jurisdictions there is a requirement for the employer, whether foreign company or locally registered corporate presence, to set up payroll in the jurisdiction at issue and to make mandatory withholdings for applicable

income taxes and social charges. This can result in significant additional employer cost. Costing this out through a payroll provider is crucial. The good news is that additional benefits are often not mandatory or expected overseas, since the statutory welfare systems will provide protections that are not necessarily common place in the US. That said, various countries (such as France, Italy, Spain and Brazil to name a few) have mandatory industry-wide collective bargaining agreements that may impose requirements to enroll employees in specific pension funds or provide yearly mandatory salary increases. Therefore, it is essential to be aware of country specific nuances.

Employment agreements and policies

Don't assume US employment templates, plans and policies will translate locally. Most countries do not have "at-will" employment. In many, written employment agreements are mandatory. Even if they are not mandated by law, employment agreements are often considered a best practice as they can incorporate crucial terms (*eg*, probationary periods, termination grounds, or working time provisions). Various jurisdictions (*eg*, Belgium, France and Saudi Arabia) require translations for the agreement to be enforceable. Duplicating the employee handbook that you use in the US is not a good idea either. US policies do not typically translate globally, an in the worst case can give employees the possibility to "double dip," seeking both contractual rights under US law plus local statutory rights. There may be no need for a handbook until you have grown significantly (*eg*, France requires internal regulations at 20 employees, Belgium requires them at 1 employee, and Japan and Korea require work rules at 10 employees), or you can use a more limited set of policies in line with what is required or expected under local law.

Manage the exit strategy

As mentioned, the concept of at-will employment doesn't typically exist outside the US (with the exception of just a handful of jurisdictions, there is nothing even close to it). Instead, all terminations require proper grounds. For instance, performance issues (which must often be carefully documented), redundancy (which often requires a look at global lack of profitability, not only a desire to restructure the role), or misconduct (which typically requires something as bad as documented bribery or proven theft from the employer). In addition, employees are typically entitled to notice, severance and some form or other of termination process. You may be left with no option other than to carefully negotiate an exit, typically with significant payouts. Releases are not enforceable in all jurisdictions either (*eg*, Brazil). Lessons learned? Implement a probationary period where permissible (and track its expiration!), carefully monitor and document performance issues early on, and simply be prepared to slow down instead of overhire.
