Home versus Host Based Pay: Benefits, Drawbacks, and Recommendations

For as long as companies have had traditional long-term expatriate assignments, they have basically followed the “Balance Sheet Approach,” which assumes that the expat will return to the departure location after a period of years and thus will remain on home based pay for the duration of the assignment.

However, in the current cost-cutting environment, companies have not only looked to structure shorter-term assignments or localize assignees, they have also looked for alternatives to replace the traditional Balance Sheet Approach and home based pay even for their traditional expatriates.

Specifically, companies are now often considering host based pay as a more cost-effective option to home based pay, including “local plus” schemes.

As discussed in this Insights, Home based pay means that the assignee remains on home country payroll for purposes of receiving base and incentive pay while assignment allowances are delivered through either the home or host country payroll. Host based pay means that the assignee transfers to the host country payroll for purposes of receiving base and incentive pay based on host country compensation practices and regulations. The company usually provides only limited, if any, assignment related allowances. Both base pay and incentive pay, as well as any above-base allowances are usually delivered through the host payroll.

Benefits & Drawbacks
Multinational companies choosing home or host based pay, as well as those using pay splits or “local plus” schemes, should be aware of the following mix of positive and negative consequences:

- **Continuation of Benefits.** One of the key advantages of home based pay is the continuation of health care, Social Security, pension, and other benefits in the home country. For assignees who will ultimately return to the home country—typically expatriates—it is critical that home country benefits are maintained. The easiest and often most compliant way to ensure continuation of home country benefits is through ongoing payroll deductions.

  Additionally, duplication of benefit contributions can be avoided. While situations may differ depending on verification by local plan administrators, setting up an expatriate on host country payroll may impose a legal requirement on the employer to offer certain host country benefits which will then have to be refunded to the assignee once he or she returns home.

  For employees who receive host based pay, benefits would ideally be determined based on host country practices and regulations. This means that continuation of benefits in these cases introduces a new element: the issue of the host country accrediting years of service in the home country and “bridging” tenure across benefits schemes.
• **Merit Increases.** For expatriates, following a home country based pay model has the advantage that the assignee’s salary progresses appropriately with home country merit increase cycles and rates. This again is critical for temporary assignments, implying that the employee will return to the home country. Basically, the assignee remains aligned with the home organization’s compensation structure while on assignment, allowing for a seamless transition upon repatriation.

On the other hand, merit increases for assignees on host based pay should follow host country practice to ensure that the assignee’s pay remains aligned with the host country compensation structure.

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• **Tax Remittance.** While home based pay delivery ensures greater compliance with home country tax remittance requirements, generally there is more of a concern with the remittance of taxes in the host country. In most instances, the assignee breaks residence in the home country and therefore home country tax remittance requirements cease for the duration of the assignment.

One disadvantage with home country based pay delivery is that host country tax remittances cannot be automatically managed through payroll withholding. Instead, where a withholding through payroll requirement exists, home country compensation data first needs to be reported to the host payroll for the subsequent remittance of taxes (“shadow payroll” reporting). Companies should be sure that their provider of compensation services provides a standardized process to ensure compliance with host country reporting and payroll withholding requirements.

So aside from cost considerations, the paramount reason for companies to choose a host based pay model has been that it facilitates the remittance of host country tax and ensures greater compliance with foreign fiscal requirements.

• **Payroll Coding.** Expatriate assignments usually provide for flexible pay delivery options from either home or host, or both locations (“split pay”).

For these types of assignments, fewer codes (wage types) are generally required if base and incentive pay are disbursed by the home country payroll, as these are already set up. Also, where appropriate, setting up one taxable and one non-taxable memo code in the host payroll for the recording of earnings may be easier than working with the host country through the set-up of detailed codes for any allowances, each requiring the appropriate tax flag setting.

In scenarios where host based pay is chosen because the employee is indefinitely assigned to the host location or localized, there is no choice but to set up the codes required for host payroll to disburse base and incentive pay, as well as potentially any above-base allowances.

• **Loss on Currency Conversion.** For expatriates, loss on currency conversion exists whether the assignee is paid in the home or the host location unless pay is split and a designated amount is disbursed in both locations. While one of the key disadvantages with home based pay is that the assignee has to convert funds to host currency in order to pay for goods and services, transportation, and potentially housing, the same issue exists when the assignee has to convert funds back to home currency in order to cover home country obligations.

The impact of loss on currency conversion on the assignee depends on where he or she is assigned and if any allowances are paid in the host country.
For localized assignees or employees indefinitely assigned to a host location, loss on currency does not really come into play, as their pay is denominated in host currency and should be adjusted to the local economy.

- **Home Country Obligations.** Lastly, as with loss on currency conversion, home country legal, financial, or other similar obligations are primarily a concern for expatriates, not localized or indefinitely assigned employees.

In the case of an expatriate, home based pay, which is more closely aligned with the Balance Sheet Approach, ensures that the assignee has the ability to meet any financial obligations in the home country more easily.

**Recommendations**

Home based pay structure and the traditional Balance Sheet Approach are still best practice for expatriate assignments because the assignment is intended to be temporary and the assignee is expected to return to the home country. With that approach, pay delivery should be split between the home and host location.

While currency restrictions and/or country-specific mandatory pay regulations may dictate the assignee’s pay delivery while on assignment, it is generally recommended that base and incentive pay be delivered from the home payroll and the following steps be taken to mitigate the loss on currency conversion and ensure compliance with host country tax requirements:

1. Where possible, make rental payments directly to the landlord.

2. Pay above-base assignment allowances in host currency:
   a. Pay housing allowance, Goods & Services Differential (COLA), and transportation in host currency (either through payroll or Relocation Accounting Services departments, and
   b. Provide an annual allowance to cover the loss on currency conversion and wire transfer fees.

3. Implement a standard pay split (as recommended by the cost of living data provider) once stabilized on a home country based pay delivery model.

4. Manage host country tax requirements through monthly (quarterly or annual) reporting to host payroll or the tax firm, as appropriate.

By contrast, localizations and indefinite assignments to the host location should follow a host based pay model for both pay structure and pay delivery. This is simply because in either scenario, it is assumed that the employee will be fully integrated into the local economy for compensation, benefits, and taxes.

**Implications of Assignment Types**

Exceptions to the above include developmental assignments and self-initiated assignments, as well as the indefinite assignment of executives.

Developmental assignments, although temporary in nature, provide companies with the opportunity to implement a host based pay approach and structure these assignments more cost effectively. This is because developmental assignments are usually geared toward a younger, less-tenured workforce that is less concerned about continuation of benefits in the home country. Additionally, developmental assignments, from the company’s perspective, represent an investment in and of themselves, allowing the employer to do away with some of the “bells and whistles” of a traditional expatriate compensation package.
Similarly, self-initiated assignments, because they accommodate an employee’s desire to go on international assignment for personal rather than business-driven reasons, can be structured based on a host based pay approach, even if they are only temporary in nature.

The indefinite assignment of an executive requires special consideration of his or her benefits, especially pension, and often complex incentive compensation in the home country. In the case of an executive’s indefinite assignment to a host location, an expatriate paradigm and home based pay may be the more appropriate choice.

**The Bottom Line**

While companies are debating home versus host based pay as a measure to structure assignments more cost effectively, perhaps the first question really ought to focus on the intent of the assignment. Defining the value proposition for an assignment should drive the selection of the appropriate assignment category and choice of pay structure.

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