Global Reward Services Quarterly Newsletter

October 2022

KPMG LLP's (KPMG) Global Reward Services Quarterly Newsletter brings you compensation and reward developments, along with KPMG observations from around the world.

Americas

United States: Termination of Tax Treaty with Hungary

The U.S. Treasury Department recently announced the termination of the U.S.-Hungary Tax Treaty. The termination will be effective on January 8, 2023; however with respect to taxes withheld at source, it will cease to have effect on January 1, 2024.

The decision to terminate follows Hungary's opposition to the Organization for Economic Cooperation and Development (OECD) Pillar Two Model Rules, which is unanimously being implemented by the European Union. It seeks to ensure that multinational companies pay an effective tax rate of 15 percent in their operating countries. However, the Hungarian parliament adopted a resolution to reject the new Pillar 2 rules, leading to effectively blocking of E.U. directive implementation. Hence, the incident may have exacerbated the Treasury's concerns about the inequities of the current treaty. Additionally, an updated treaty is pending for approval in the U.S. Senate since 2010.

For more information, read our KPMG Flash Alert.

KPMG observations:

Due to the termination of the U.S.-Hungary Tax Treaty, the benefits of lower tax rates on certain income (interest, dividends), exclusion for certain employment income, and relief from double taxation will no longer be applicable. This could lead to a rise in double taxation, without relief for individual taxpayers. It may also lead to higher international assignment cost for mobility programs.

United States: SEC adopts final pay versus performance disclosure rules

On August 25, 2022, the Securities and Exchange Commission (SEC) approved the final rules implementing pay versus performance disclosures under Section 953(a) of the Dodd-Frank Act rules. These rules will be applicable for the upcoming 2023 proxy season. At a high level, the final rules will require the following for each of the registrant's last five completed fiscal years:

- Tabular disclosure of executive compensation levels are as follows:
  - Total compensation for the covered fiscal year as reported in the summary compensation table for the Principal Executive Officer (PEO), and the average total compensation as reported in the summary compensation table for the non-PEO named executive officers.
  - The actual compensation paid to the PEO, and the average actual compensation paid to the non-PEO named executive officers. This is calculated as total compensation reported in the summary compensation table with adjustments for amounts related to pension value and equity awards.
- Tabular disclosure of the following financial performance measures:
  - Initial fixed investment of amount $100 based on Total Shareholder Return (TSR) for the registrant and TSR for the registrant's peer group.
  - Registrant's net income.
  - Company-Selected Measure, which represents the most important financial measure used by the registrant to link compensation actually paid to the named executive officers.
- In addition to the above, the registrant is required to provide:
  - A tabular list of the most important three to seven financial performance measures. The list may also include non-financial measures, if they are deemed as 'most important' by the company
  - A narrative on the relationship between:
    - » the compensation actually paid and the TSR
    - » the compensation actually paid and the net income
    - » the compensation actually paid and the Company-Selected Measure
    - » further, also provide a comparison of cumulative TSR of the registrant and cumulative TSR of the registrant's peer group

- Effective timing: The new disclosure will be effective after 30 days of publication of the final rule in the Federal Register. Registrants need to comply with the new requirements in proxy statements for fiscal years ending on or after December 16, 2022, with an interactive data format.
  - Registrants can disclose three years of information instead of five in the first released proxy statement.
  - The new disclosure is applicable to all reporting companies except for emerging growth companies, foreign private issuers, and registered investment companies. Furthermore, smaller reporting companies are subject to reduced requirements.

KPMG observations:

As the proxy season approaches, management teams should set aside extra time and resources to coordinate with the Compensation Committee when preparing internal and external communications (including the proxy disclosure) that address their executive compensation levels and their correlation to the company's financial performance. Registrants should be methodical in the placement of the disclosure, how it may impact the Compensation Discussion & Analysis, and whether any supplemental or voluntary disclosures may be necessary.

Asia Pacific

Hong Kong : Important court decision on equity-based compensation

On July 22, 2022, Hong Kong's Court of Appeal issued a decision related to equity-based compensation that dismissed the Commissioner's appeal and upheld the lower court's decision in favor of the taxpayer. The taxpayer in this case relates to a person who was employed by a bank in the U.K. from 2002 to 2014. The taxpayer was transferred to another company within the bank's group in July 2014 and was employed under a Hong Kong employment contract henceforth.

The court determined that the awarded shares were related to the taxpayers performance while employed in the U.K. and, therefore, are not considered income earned in Hong Kong. Additionally, the court determined that the share dividends are non-taxable, as they are income from shares and not income from employment.

The Court of Appeal confirms the distinction between:

- Shares awarded by an employer that are subject to vesting conditions to be met before an employee becomes the legal or beneficial owner of the shares; and,
- Conditions that may cause a later forfeiture of shares that are transferred to an employee (or to a nominees for his/her benefit) upon grant.

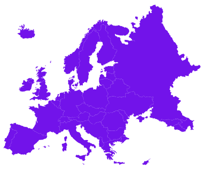
The decision is important as it draws a clear distinction between a vesting period, which defers accrual of the income, and an outright grant with the possibility of forfeiture on the occurrence of a future event.

For more information, read our KPMG Flash Alert.

KPMG observations:

The distinction between vesting and forfeiture clarified by the Hong Kong courts is different from the tax position in other jurisdictions, which may consider the employment income as arising only after the risk of forfeiture has lapsed. Employers should consider whether this distinction impacts their current equity plans and also take this into consideration when making future equity award grants to Hong Kong participants.

Europe



European Union: Extension of COVID-19 measures for social security

On June 14, 2022, the European Union Administrative Commission (the Commission) further extended the ‘no-impact policy’ related to social security for frontier workers until the end of 2022. The Commission notes that this is a transitional period that will allow people that are covered by the ‘no-impact policy’ to adjust with the change. It allows the workers who reside in one E.U. member state and work in another E.U. member state to avail work from home for more than 25 percent of the time while remaining covered by social security in the country where their employer is located.

The policy, introduced during the global pandemic lockdown, aimed to avoid change to applicable social security laws related to cross-border workers. The ‘no-impact policy’ was introduced for a period of six months, with further multiple extensions. The most recent extension will last until the end of 2022.

For more information, read our KPMG Flash Alert.

KPMG observations:

The extension to the ‘no-impact policy’ allows the frontier workers to continue with work from home without becoming subject to social security in their country of residence. It is expected that remote working will be considered as a view towards more permanent changes for coordinating rules for social security.

Finland: Proposed exit tax for individuals

On August 12, 2022, the Finnish government published a preliminary draft of a proposal for an exit tax that would lead to a significant expansion of Finland’s right to tax the assets of wealthy individuals who move abroad. The purpose of the exit tax is to increase tax revenue, by closing a loophole that allows the individuals with assets that have increased in value to move to a country that has lower or no tax rates for capital gains, and then sell the assets with minimal tax consequence. Capital gains in Finland are taxed at a rate between 30-34 percent. Exit taxes were already in use in Finland for corporate taxation and certain stock share exchange situations, however, they were not applicable for private individuals.

The non-real estate types of income that would be subject to the exit tax includes company shares, shares in national and foreign investment funds, options, futures, capital redemption policies, endowment insurance, pension insurances, and virtual currencies.

The exit tax is applicable to individuals who:

- Before moving from Finland have had their tax treaty residence and have been tax residents, as per national law in Finland for at least 4 years of the previous 10 years
- The value of the individual's assets, on the date before the individual moves from Finland, must at minimum be valued at EUR 500,000, and have a EUR 100,000 hypothetical capital gain

The income that is subject to the exit tax is considered as income in the tax year when the individual moves from Finland. The individual has the right to postpone the payment of the tax until the assets are disposed of in a sale or gift. The exit law is not applicable, for the assets not disposed of for 8 tax years following the year when the individual moved away from Finland.

For more information, read our KPMG Flash Alert.

KPMG observations:

The proposal for the exit law is to come into force at the beginning of 2023. To understand the impact of the proposed exit tax, the employers need to review cases where a Finnish individual is sent on assignment abroad or a foreign employee relocates to Finland.

The proposal seems to have far-reaching consequences for situations which were earlier overlooked like long-term assignments to Finland of executive-level employees. The tight schedule of the legislation may also lead to uncertainty and faces significant criticism from interest groups and experts.

Netherlands: Dutch cross-border agreements with Germany & Belgium

Due to the COVID-19 Pandemic, the Netherlands came to separate agreements with Germany and Belgium that applied a certain degree of leniency when taxing cross-border employees. Workers who would have normally commuted from the Netherlands to Germany or Belgium may have had to work from home during the pandemic. Therefore, as of March 2020, employees who performed their work in the Netherlands because of COVID-19 restrictions were deemed to have spent that time working in the country that they would have worked in the absence of COVID-19. However, this did not apply to employees that were not disrupted by COVID-19 restrictions and had been working in their home countries regardless of COVID-19.

As of July 2022, both mutual agreements no longer apply. As a result, employees who perform their work in their home country, from that date, will not be deemed to have spent these workdays in the country where they ordinarily would have worked in the absence of COVID-19 and will be taxable in their home country for any home-country working days.

Employers therefore might need to reconsider, and change, the current payroll administration.

For more information, read our KPMG Flash Alert.

KPMG observations:

Employers that have workers still operating in The Netherlands will need to account for the different set of administrative obligations and compliance requirements that would not have been present if the employees had been working in Germany or Belgium. Employees will also face different tax obligations if they do not return to working in their host/commuter country office location.

Switzerland: Extension of Pandemic-Related Tax Rules for French Cross-Border Workers

France and Switzerland extended the agreement to enable work from home for French cross-border workers with Swiss employers across all cantons with cross-border rules, with the recent deadline as June 30, 2022.

The announcement follows Switzerland's agreement with the European Union to continue flexible application of social security rules for remote workers until December 31, 2022.

For more information, read our KPMG Flash Alert.

KPMG observations:

France and Switzerland recognize the emergence of work from home and are in agreement to redefine tax rules which reflect the new reality. The extension aims to facilitate more time to both countries to conclude a new agreement which is 'supple, simple and fair' for employees and employers alike, and allows for an equitable split of tax revenues between the countries. Further, they are committed to finding a solution before the end of October 2022.

Additionally, the authorities plan to find a permanent solution regarding the misalignment of tax and social security rules before expiry of extension date.

Switzerland: Legislative update on special tax and social security regulations for COVID-19

The Swiss government recently announced changes to the social security rules for remote workers that will last until December 31, 2022.

In response to the pandemic, related border closures, and widespread working from home, several tax and social security related agreements have been concluded and extended to coordinate taxation and social security rules for frontier workers.

Key changes include:

- **Taxes**
  Switzerland concluded consultation agreements with Germany, France, Italy, and Liechtenstein on the taxation of foreign workers, particularly the cross-border commuters who used their home office as their physical place of work. Switzerland extended Tax agreements with France and Italy (until October for France and until further notice for Italy). The agreement with Germany and Liechtenstein ended in June 2022 and March 2022, respectively. There was no mutual agreement concluded with Austria.
- **Social security**
  The European Union's proposal to maintain the flexible implementation of social security laws for remote employees through December 31, 2022, has been accepted by Switzerland. The common norms of EU regulation 883/2004 will apply if these regulations are not extended as of January 2023.

KPMG observations:

Due to the end of the specific agreements regarding cross-border employees with Germany and Liechtenstein, Swiss employers are currently implementing, or have implemented work-from-home policies should consider whether these policies may result in foreign tax exposure and related reporting obligations. The European Commission is currently in conversation with the OECD for possible coordination of the differential taxes of cross-border teleworkers within the European Union and between OECD member states, which currently are incongruent.

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