Taxing global staffers

BEST SOLUTION MAY LIE IN TAX EQUALISATION BENEFIT ARRANGEMENT WITH EMPLOYEES

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IN THE MODERN ECONOMY, WE FIND FREE movement of people and goods across various nations. The cross border movement of people to render services may give rise to tax obligations to such individuals in more than one country. The local tax laws and double tax treaties entered into by the governments generally provide for tax exemption to short-term travellers in the visiting country (host country) who stay for a period ranging from 30 days to 180 days in the relevant tax year.

When an international traveller stays for more than the minimum period in the host country or fails to satisfy the conditions for claiming the tax exemption, the host country tax laws will apply to such travellers. As this tax obligation arises on account of performance of duties in the course of employment, it is natural that the employer will try to appropriately compensate the employee for such additional tax liabilities.

Employers adopt different approaches to compensate and support the employee on host country tax obligations. This may also at times involve changes in the payroll delivery model of employees based on the tenure of the employee's overseas assignment. This could take either of the following forms:

Transfer of payroll: Under this model, the employee will receive the salary in the host country and his salary will commensurate with the entitlement of the employees of the host country who are in the same employment grade. In this arrangement, invariably, the host country tax liability will rest with the employee. This structure is adopted primarily for long term assignments extending for more than 12 months.

Split payroll: This model involves dual pay structure whereby the home country (the country of original employment) will pay the base salary and the host country will pay allowances to cover the cost of living. The company may also top up the host country allowance to cover additional taxes. This deliver model is adopted for assignment with less than 12 months.

Home Country Payroll: Under this structure, the employee's payroll with additional assignment compensation will be fully delivered in the home country buffered with tax equalisation benefit arrangement to the employee.

> India may need to amend the Companies Act to permit tax-free salaries and facilitate tax equalisation

The concept of tax equalisation has been in vogue in most of the overseas jurisdictions. This is a benefit extended to the employees who are on international assignments essentially to shield them from uncertainties associated on host country tax obligations. This benefit works in such a way that the employee will be asked to shell out the money towards taxes only to the extent that he would have to pay in the home country on specific salary components if he had not undertaken the international assignment. This deduction is termed as "hypo tax" in international parlance as this represents only the hypothetical tax which the employee would have paid in the home country and not actual tax. The employer will pick up the host and home country tax liability of the employee. This arrangement will ensure tax neutrality to the employee.

Looking at this aspect from employer perspective, the employer will bear additional taxes if the host country's tax rate for the employee is higher than the home country but there will be savings if the host country's tax rate is lower.

In India, the concept of tax equalisation is gradually receiving attention and it is likely that the companies that like to emulate global best practices on employee matters may evaluate the option of introducing such benefit schemes for their international travellers. The laws in India particularly the Indian Companies Act which restricts payment of tax free salary to employees may also need to be amended to facilitate introduction of this concept.

(The author is leader, Global Employer Services, Deloitte in India)

debate What beleaguers air safety in India?

V THULASIDAS | FORMER CMD, AIR INDIA

Safety concerns are overplayed, flying is safe in India

THE MANGALORE AIR CRASH HAS THROWN up questions regarding air safety in India. It is but natural that a tragedy of this proportion will invite public and media attention to the negative aspects of Indian aviation. It is, however, unnatural, and typically Indian, to imagine all possible horrors and see an accident in every flight that takes off.

Is aviation in India worse than rail or road transport in terms of accidents and fatalities? Scan any newspaper almost any day, and you will read about crashes, on either the roads or rail lines. Are those deaths less painful or less important?

Let us concentrate on all the negatives in an attempt to improve air safety in India. But, this need not be done by imagining near misses all over Indian skies. Is it that, even if true, these happen only in India?

A quick internet search shows that in 2009 and 2010, till now, there were six accidents in the USA/US aircraft, three each in Indonesia and Iran and two each in India and Dubai/Dubai aircraft and one each in 14 other countries. The Air India Express crash is the third highest in terms of fatalities, after 228 deaths in the Air France crash in the Atlantic and 168 deaths in the Caspian Airlines crash in Iran. There were 52 deaths in the case of US. It is pure luck that the passengers of the US Airways flight that ditched in the Hudson river did not drown.

The Air France crash of June 1, 2009 does not make France an unsafe country for air travel. If frequent accidents and fatalities happen, that certainly casts doubts on safety standards in a country. The last fatal crash of a commercial airline in India was the Alliance Air crash in July 2000 in Patna.

The reason for any accident needs to be understood before we start the blame game. Investigation in to the Mangalore crash will bring out the reason. The earlier it is done, the better. It is important, thereafter, that the agencies concerned, government, Director General of Civil Aviation (DGCA), airline and airport take corrective action, promptly and transparently. This alone will send a reassuring message to the travelling community.

> DGCA needs to keep pace with the growth in the aviation sector. Air travel is a safe mode of transportation

Knee-jerk reactions from any quarters, prompted by frenzy on TV channels or prophets of doom, should not dictate policy or corrective action. For example, the environmental lobby baying for blood for the construction of the second runway in Mangalore or the lobbies demanding ouster of all foreign pilots wholesale or the impression sought to be created that a table-top runway is essentially unsafe, are all to be taken with a pinch of salt. The regulator in India, the DGCA, has been in the forefront of enforcing safety standards. True, India can do with better technology, more sophisticated equipment and more skilled manpower. After all, Indian aviation grew too fast, perhaps, in the last 5-6 years, and the regulator also needs to grow. But, let us not send wrong signals to the international community that Indian aviation is not safe; it is safer than that in most other countries. It is safer than other modes of transport in India.

SANAT KAUL | CHAIRMAN IFAAD* (INDIA CHAPTER)

DGCA lacks both financial and technical independence

IS SAFETY OF OUR CIVIL AVIATION SET-UP IN good hands? Is the safety apparatus adequate? These are some of the questions in the mind of the public after the Mangalore crash and the reports of 'near-misses' happening on a daily basis. After Mangalore crash, there have been a series of near misses such as a tyre burst in Delhi, a go-around at Patna airstrip and sudden descent over Muscat while the pilot took a toilet break.

These are signs that our safety apparatus is under stress. While we cheered and gloated over the growth in civil aviation, new aircrafts and new or refurbished airports, little attention was paid to safety surveillance. Alongwith growth of aviation, it is essential to ehance the safety systems. In India the reverse happened. We gloated over growth and forgot the safety. As a result, we did not even fill up essential safety posts. With posts lying vacant over a year, they attracted the across-the-board ban on filling vacant posts when permanent economy cuts were imposed by the finance ministry. In 2006, International Civil Aviation Organization rated India poorly in its safety audit. Finally, it was the threat of a downgrade from category-II country to category-I by Federal Aviation Authority (FAA) of US that led to a prime ministerial intervention and creation of posts.

> Accidents should be probed by an independent statutory authority similar to the NTSB of the US

We need to clarify where the buck stops and who are the stakeholders. At one end is the Director General of Civil Aviation (DGCA), the safety regulator. The second is the Airports Authority of India (AAI), which has the statutory charge of air traffic management and are, therefore, the sole service provider for air traffic management. Third is the ministry of civil aviation. Both the DGCA and the AAI are subordinate to the ministry. The only difference is that AAI is an independent authority with its own finances and its chairman and executive directors are appointed by the Public Enterprises Selection Board. DGCA, is, unfortunately, an attached office of the ministry with very little financial and non-financial powers. The budget of the DGCA is a part of the ministry's budget, and therein lies the problem.

The lack of independent status almost cripples the DGCA. Unlike in other countries such as the US where the FAA comes under the Department of Transport but is independent by tradition and statute, DGCA appointments are an internal matter for the government. This puts DGCA at a disadvantage. All essential matters have to be referred to the ministry. All accident reports have to be approved by the ministry. He cannot create even a post of peon.

It is high time that DGCA was made into an independent authority with financial independence and with power to create technical posts and fill them up. Without such independence, issues of surveillance over safety oversight in aviation will remain a pipe dream. Further, the issue of accident investigation (including near-misses) should be with an independent statutory authority similar to National Transport Safety Board of the US, an autonomous body for all transport modes including the railway and roads, and kept independent of the government.

**International Foundation of Aviation, Aerospace and Development*

Teaching macro economics needs course correction

RESEARCH grey matter EXPLAINED

FOLLOWING the 'Great Recession' of 2007-09 in the mature economies abroad, there's much talk of proactive change in the offing. While the Obama administration continues to mull over policy reform in response to the recent financial crisis, the mavens have begun to think aloud about changes likely in pedagogy and textbooks. A recent working paper at the Center for Economic Policy Studies in the US is about teaching macro-economic principles after the financial crisis. What's posited is much more emphasis on business cycles, a 'healthy dose of Keynes', read government intervention in the short-term to prop-up demand, and fundamental re-thinking on 'standard macro models' and especially the simplifying assumption of the 'one-interest-rate' model. Phew!

Now the financial crisis happened in the US and elsewhere basically because of massive recourse to "structured products," especially the issue of mortgage-backed securities. Such securitisation, in theory, implies fanning out and spreading wide the risks of payment default, and so seem attractive. And especially so against the backdrop of rising house prices. The presumption was that in the event of a default on mortgage payment, the house would simply be resold at a higher price. Note also that mortgage finance in the US is generally 'non-recourse,' with borrower liability limited to the property per se and not linked to borrower income. It was perverse incentive to seek out sub-prime borrowers, with dicey credit history and often with little or no steady income.

And back-to-back, the mortgage receivables were securitised at relatively high interest rates — in a general regime of low cost of money. More important, in the process, there was massive recourse to leverage and borrowings by the finance players. When the housing bubble burst in the US, it led to large-scale defaults on mortgages, and the tens of billions worth of mortgage-backed paper because of dud securities overnight. The 'toxic assets' led to a credit freeze, global financial crisis and precipitated the mega-recession. It's current history.

The paper says that in macroeconomic texts the relative degree of emphasis on growth needs to make way for more analysis of business cycles. In the cavalier 1990s, 'growth became the rage and cycles were submerged,' notes the paper. Given the real prospect of subdued growth in the mature economies going forward, renewed stress on business cycles phenomenon seems likely. Also, more textual emphasis on Keynesian intervention as a policy instrument to boost effective demand is required, says the paper. Otherwise, it would be 'pretty hard' to explain recent government responses and unprecedented loose fiscal policy the world over, it is averred. Further, what's required is rethink on the standard, textbook assumption of one-interest-rate models. To explain recent events, such constructs would need to be dropped, it's surmised.

Additionally, what's called for is more textual emphasis on financial stability; the focus hitherto has overwhelmingly been on macroeconomic stability read lower inflation, easier cost of funds etc. It can mean downplaying the effects of asset price bubbles as the crisis did amply demonstrate, it is noted.

The study goes on to enunciate that new topics need to be introduced, in the light of the financial crisis, for example the idea of risk premiums in interest rates. After all, in the run up to the crisis, the rates on mortgage-backed paper soared, while those of treasury bills literally approached zero in a general regime of low interest rates. Post crisis, what needs to be hammered home is the fact that higher likelihood of default show up as higher risk premiums. Besides, the negative implications of asset-market bubbles do need to be factored in. It is clear now that house prices in the US went way beyond fundamentals before the crisis, and the subsequent burst had very severe implications. Concepts like securitisation, leverage and illiquidity all need to find mention in textbooks, concludes the paper.

(Teaching Macro Principles after the Financial Crisis, by Alan Blinder, CEPS working paper 207, Princeton, April, 2010)

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No easy way to regulate microfinance

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COMPLEXITY IS BEDEVILLING THE INDIAN government's attempts to regulate the microfinance sector.

In recent months, there has been a flurry of reports about some microfinance institutions (MFIs) offering loans to women without ascertaining their ability to repay, about their staff coercing repayments, about women taking multiple loans to keep up with onerous weekly repayment schedules, etc. It also seems that while MFIs' portfolios are swelling, their system to manage that money have not kept pace. Ramesh Arunachalam, a microfinance consultant, says the industry doesn't have half the systems that even the RRBs did. Other developments, like the decision by SKS Microfinance's top management to sell all their shares (barring ESOPs they could not exercise) to a Hong Kong hedge fund a month before the MFI filed its draft red herring prospectus, have alerted regulators about corporate governance in the industry.

For all that, the government is taking time to decide how to regulate microfinance. This is partly because it does not want to do something that chokes the flow of microcredit. And partly because of complexity.

The Indian microfinance industry is characterised by a multiplicity of microfinance providers dispersed across the country. These players belong to diverse institutional forms — NBFC-MFIs, cooperative societies, not-for-profit companies (under Section 25 of the Companies Act, 1956), trusts — all answering to different laws and regulations. The nature of the business itself, built around several small cash transactions at the last mile, makes it almost impossible to verify claims about collection methods and interest rates without onsite supervision.

This complexity is nobbling attempts to regulate the sector. Take the RBI. Earlier this year, it was suggested the central bank regulate MFIs by capping the interest they can charge, or through its NBFC norms (several of India's for-profit MFIs are NBFCs) or by linking priority sector lending benefits to MFI behaviour. But, asks RBI deputy governor KC Chakrabarty: "How can the RBI know what is the right interest to charge across the length and breadth of India?" Nor have the other suggestions passed muster. NBFC regulation is meant to ensure that the

> Nabard and the finance ministry are grappling with the question of how to regulate the MFIs. A Bill to regulate MFIs is back in consideration

NBFCs do not pose a systemic risk, he says, whom they lending to, at what rate, how they lend, etc, does not come under the RBI's purview. Even if the priority sector lending status is revoked, that will result in banks lending to MFIs at a higher interest. And they will in turn lend at still higher interest. Also, he says, "All MFIs are not doing a bad job. Also remember, if no MFI gives her money, the borrower will be under even greater hardship."

Nabard and the finance ministry are grappling with similar questions. Over the past couple of months, both have been inviting comments, again, to the Draft Micro Financial Sector (Development and Regulation) Bill. This Bill, it will be recalled, had been first tabled in the Parliament in 2007 but it lapsed without becoming an Act. Since then, it has been on the backburner due to several reasons — the industry was split on the bill, it is not clear whether microfinance should have its own legislation or be governed under the same norms as banks and NBFCs, whether non-financial bodies like societies and trusts should be allowed to accept deposits.

Today, Nabard and finance ministry are facing these and other questions. How, given the thousands of microfinance providers operating in distant corners in India, can Nabard (which is named regulator in the microfinance bill) keep tabs on them? There are questions about conflict of interest. Nabard backs the self help group (SHG) model. And some of the largest MFIs, says Mr Arunachalam, have grown by cannibalising SHGs.

Worse, the bill was written to supervise institutions accepting deposits from microfinance clients — trusts, charitable societies, non-profits, etc. Which excludes NBFC-MFIs and cooperative societies from its remit. But does the Bill makes sense if NBFC-MFIs are beyond its purview? For, while the non-NBFC MFIs comprise 80-90% of all microfinance providers, they account for no more than 26% of the overall loan portfolio. Similarly, should member-societies be brought under the purview of the bill?

The fact that microfinance providers are registered under different laws with different regulators poses its own conundrums. No one regulates the financial operations of charitable societies. Conversely, while the RBI monitors NBFC-MFIs' financial operations, it doesn't monitor their lending practices. This, says Nabard executive director Prakash Bakshi, is "a black hole. We are not able to decide on this." One answer might be to entrust Nabard with both roles. But that is another question awaiting resolution between RBI, Nabard and finance ministry.

At this time, one viewpoint inside Nabard is that the Bill should only lay down prudential guidelines for the industry. And mandate that all microfinance providers, regardless of whether they come under the purview of the bill or not, have to register and file their returns with Nabard. This viewpoint holds that the industry's behavioural problems are best resolved by the industry itself through information-sharing, etc, and that governance at most microfinance providers will improve once the guidelines are laid down.

At this time, Nabard has passed a consolidated list of feedback to finance ministry.

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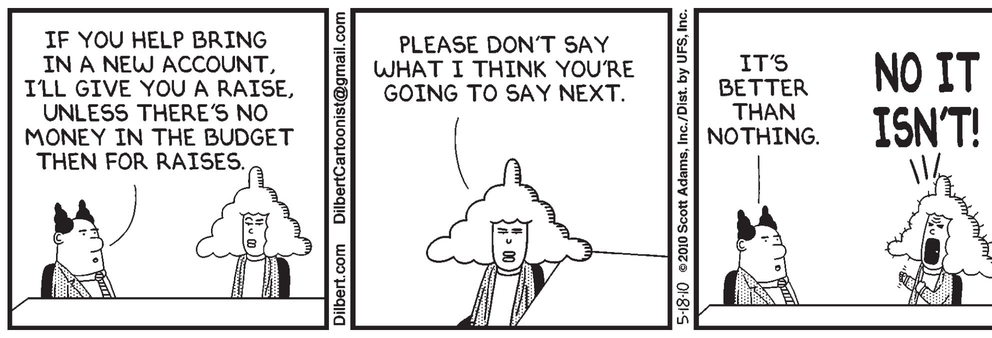
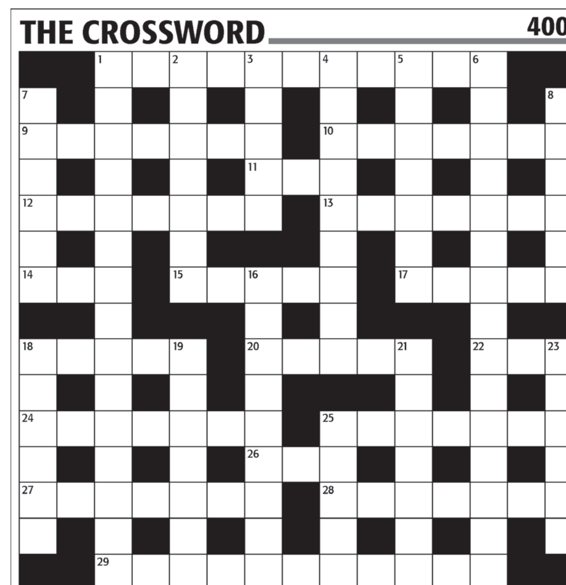
DILBERT by S ADAMS



THE CROSSWORD 4002



ACROSS

1 Pose for gear that could appear in some sort of paper (11)
9 Dine in the home that's best prepared (7)
10 Force out afterwards without starting to be offensive (7)
11 Still until now (3)
12 One has to check out raid damage (7)
13 Leave music playing (7)
14 Negative return at high speed (3)
15 Cancel it after radiation dosage (5)
17 It adds up to a lot of trouble after starting time (5)
18 One of those up for approval (5)
20 Ready to go to bed dressed (5)
22 Away when not working (3)
24 Adjust rise owing what's left (7)
25 China's awful nemesis (7)
26 Top performer one may take in hand (3)
27 Letters to dispatch for a distant settlement (7)
28 They're applied to soothe fools who've taken it back inside (7)
29 Land in trouble in a love that throws out sparks (5,6)

DOWN

1 Do rag Sir Quintin about heading a religious tribunal (5,10)
2 The one he approves of gets cross (7)
3 He chases women one day a year (5)
4 Versifier advertising tea blend inside (9)
5 Vagabond players released from prison (7)
6 One may have a layer of distinction before the build-up (10-5)
7 Young admirer in the turn-out (6)
8 Found in a low tavern a little later in the spring (6)
16 Damaged people filled with Biblical anger (4-5)
18 Turn to dry wine when you have fish (6)
19 Head down here after retirement (7)
21 Hadn't the power to keep going (7)
23 Perfection at last! (6)
25 Toast to a singer (5)

Solution to 4001

ACROSS: 1 Call sign, 5 Sample, 9 Luminous, 10 Hawser, 12 Mind, 13 Economical, 15 Price increase, 19 Barefaced liar, 23 Tremendous, 25 Java, 28 Agenda, 29 Pleasant, 30 Tweedy, 31 Usefully.

DOWN: 1 Column, 2 Lemon, 3 Sand, 4 Gouache, 6 Alarm, 7 Push-chair, 8 Enrolled, 11 Anon, 14 Tiff, 15 Persevere, 16 Ire, 17 Rain, 18 Abstract, 20 Code, 21 Douglas, 22 Pantry, 24 Ended, 26 Avail, 27 Half.

The Daily Mail