papaya global

The Ultimate Guide to EoR

A unique model for more efficient, compliant overseas employee management

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What is an Employer of Records?

The world has got a whole lot smaller in recent years, with many organizations expanding their search for workplace talent outside of their home country. In order to legally take advantage of highly-skilled candidates from anywhere in the world, these organizations would traditionally need to set up an entity in the location that the new employee will be working, also known as incorporating locally. Setting up a legal entity is no easy task. It comes with many tax obligations and legal liabilities. These include end of year financial reporting, the nomination of local directors, and the necessity to prove that you are meeting numerous local legal requirements.

When you want to onboard a new hire quickly, it can be a real bottleneck, as in some cases it can take months to set up the entity before you can officially onboard the candidate onto the payroll. Once set up, your organization will need a lot of expertise on areas as broad as compliance, tax, benefits and pensions in the new location, all while keeping a new hire satisfied, and settling them into your company culture from a distance. Importantly, if the new hire doesn't work out, and you decide to close the entity, this can often be as time consuming and expensive as setting it up in the first place.

An Employer of Record is a simpler and smarter route to the same outcome. You can hire candidates anywhere in the world, taking your pick of the best talent, but the actual payroll management is outsourced to a local partner, who hires the candidate on your behalf.

The EoR will be both responsible and liable as the employer of record, while on the employee side they will see no difference, working for your organization the same way they would as a locally-based employee.

If you choose to partner with an EoR, you can expect them to handle:

- Payroll, in compliance with local government agencies and laws
- Tax obligations, including handling both employee and business taxes
- Benefits, including insurance, pension schemes, global equity, and often, perks
- Elements of HR, including working hours, vacation days and sick leave
- Drafting of locally compliant employment contracts

A note on terms

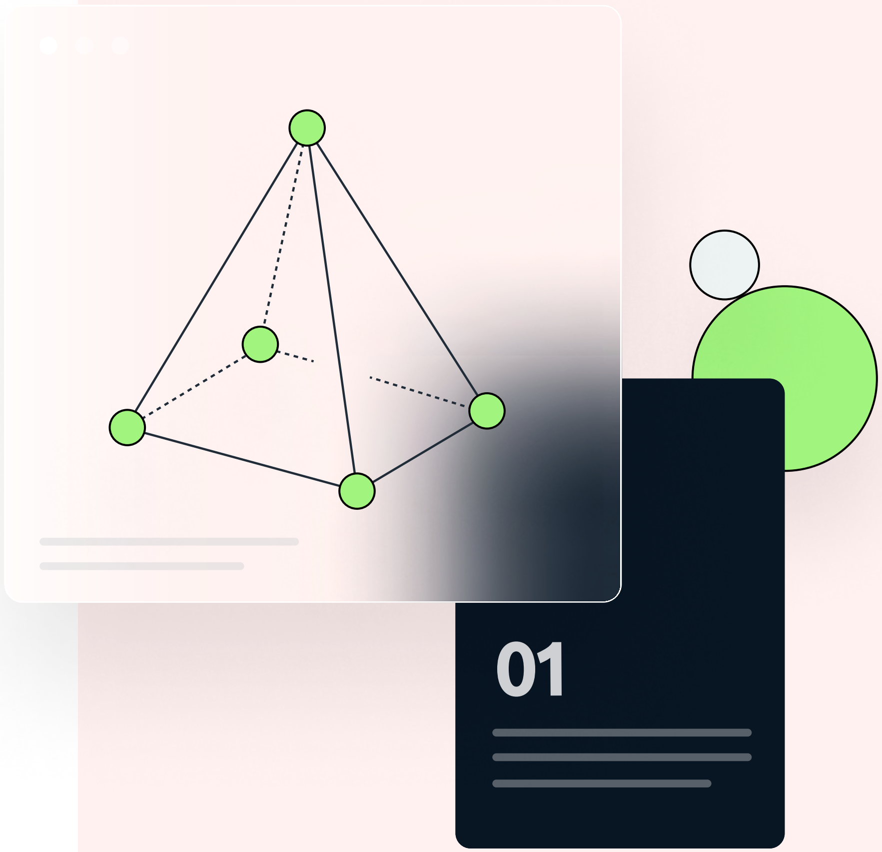
EoR stands for Employer of Record, globally recognized to mean a situation where a third-party takes on specific tasks and processes related to employee management. You may also hear the term Global PEO, which stands for Global Professional Employer Organization as well as GEO, Global Employment Organization.

Essentially, these terms all refer to the same type of services. One difference, found in the US, is that the term PEO can be used to refer to a model of employment where the PEO works within the United States, and manages certain employee services on an organization's behalf.

This version of a PEO arrangement can be used to get organizations a better deal on elements of employment such as insurance and benefits. This is not to be confused with EoR, which can also be called Global PEO, and is focused on facilitating business expansion overseas.

Examples where this model is perfect, include:

- **Hiring a candidate in a new location:** EoR lets you onboard the best talent in a new location in an inherently compliant way, without setting up an entity.
- **Testing a local market:** Think of EoR as a low-risk, ‘try before you buy’, allowing you to see if a new location is a good fit before incorporating.
- **Short-term engagement:** Sidestep the admin of opening an entity by using EoR, leveraging short-term relationships with any candidate, anywhere.
- **Handling an interim solution:** EoR is a great way to fill the gap if you’re waiting for your entity to become official, allowing you to start working faster.



Why not utilize the contractor model?

You might be asking yourself, why not just allow remote employees to come on board as freelancers? If so, you’re not alone.

According to a study by Deloitte, up to 33% of organizations rely extensively on the gig economy, which includes freelancers, contractors and other forms of alternative labor.

As a freelancer is responsible for their own employment, you can see why organizations could see this as a great way to avoid the need for local expertise in areas such as benefits, tax and compliance.

However, worker misclassification for contractors is a growing problem, and one which can seriously cost your business in the long run. This occurs when you are calling a worker a freelancer or a contractor, but in actuality, you are treating them as an employee.

However, in general terms, ask yourself these questions:

1. Does your contractor have a long-term working agreement with you?
2. Is it difficult to define their tasks as isolated work projects?
3. Do you control their hours, location, or rates?
4. Are you their only client?
5. Does the majority of their annual income come from your company?

If the answer to any of these is yes, you might be in danger of breaking classification rules.

Determining whether you're misclassifying your workers is no easy task. In the US, for example, the various levels of federal, state, and local government agencies each have their own definition of employee and freelancer.

This potentially puts organizations in the strange position of being compliant with one standard, and liable by another.

What makes misclassification mean in practice?

Under Federal and State law, if you're found to have misclassified workers, you may need to pay 100% of the employment tax back to the government, as well as federal income taxes, social security taxes, and 6.2% of unemployment tax. Under the Federal Fair Labor Standards Act (FLSA), employers can be held liable for failing to pay for overtime, or for sidestepping minimum wage requirements through using freelancers.

In severe cases of misclassification, organizations might find themselves involved in a class action suit by their workers. In one high-profile example, FedEx had to pay out $228 million after attempting to save on labor costs by misclassifying its drivers.

Other dangers of working with contractors instead of employees are:

Intellectual property

Under standard copyright law, rights to any content are held by the person that creates them, so this needs to be waived in a written contract before the work can be handed over to your organization and considered your own.

Motivation

It's important to take some time to consider the social risks to utilizing a freelance model for employment as well. Freelancers are likely to show less loyalty and connection to your brand.
For many companies expanding globally, building a company DNA is key, which is likely to be hampered by making use of freelancers.

Non-compete

It can be hard to enforce clauses such as non-compete or non-disclosure with regards to freelancers. In fact, the very act of asking a freelancer to sign a noncompete may be enough to convince compliance regulators that this worker is in fact more of an employee than a contractor.

Privacy and compliance

By their very definition, freelancers are likely to be working within the same industry with competitors or industry partners. In this situation, confidentiality can be an issue, even if a freelancer has signed an NDA. After all, how can you ensure that the knowledge they're learning from working with you doesn't help them add value elsewhere, even with the best of intentions?

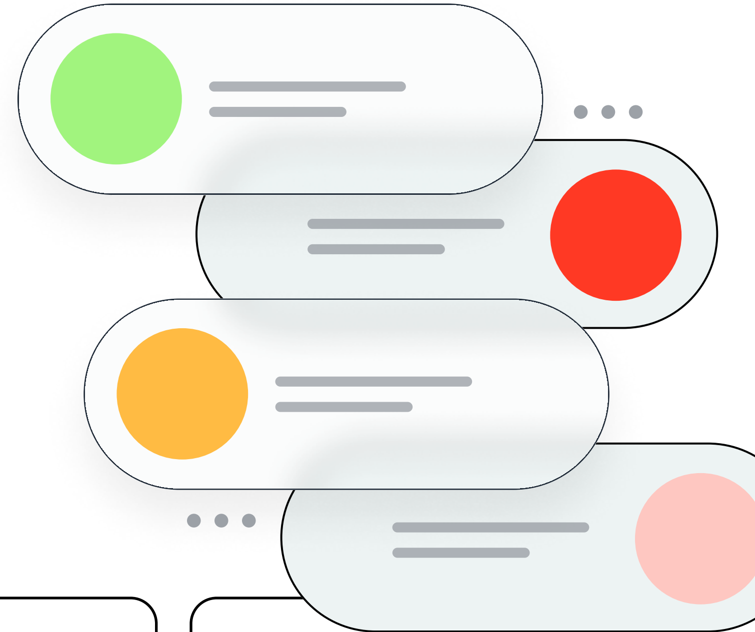
Financial uncertainty

As the control is in the hands of the contractor, it can be tough to adequately forecast ahead of time how much your employment costs will be. There's also an element of added expense in managing freelancers, including varied pay schedules, currencies, and costs.

While the contracting model may work for niche, short-term requirements, it is not a solution that can allow you to shortcut hiring overseas employees – not without taking on a lot of risk at the same time.

The four key benefits of using an EoR

Breaking down the benefits of EoR



Flexibility

Hire full-time employees in any location risk free, without having to set up an entity, or worry about misclassification. Hire employees that can get the job done, creating a broader pool of talent.

Time

When it comes to hiring the best talent, time is of the essence. Leapfrog the competition and scale quickly, putting workers in place anywhere globally, in a fraction of the time it talks to hire via traditional means.

In-Country Awareness

No need to learn local customs regarding payment benefits. Instead, place the compliance requirements and payroll processing in the capable hands of local partners.

Cost

Hire international workers without going through the expense and headache of setting up a local, permanent entity, including registration and incorporation fees for every country in which you have employees.

7 things to consider when choosing the right EoR provider

Knowing that EoR is the right employment model for you is just step one. The next part of the process is working out which EoR provider suits your business needs. Here are 5 questions to get you started.

01 Does the EoR have a local presence?

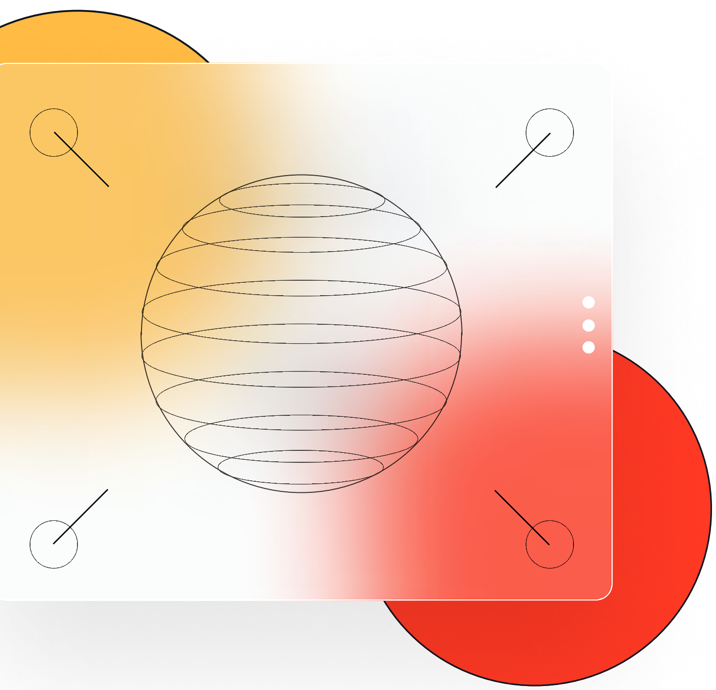
Every country is different, and will have their own laws, compliance regulations, culture, and expectations around the employer/employee relationship. To be sure of compliance in a foreign market, and to get started with your best foot forwards, the EoR has to have a local presence. That means either the EoR itself is based in the country where you are hiring, or it needs to be associated with an in-country partner to handle workforce management. Without a local presence, a company can easily fall behind with changes to legislation that could affect your company directly.

They also might not be experts on various details of workforce management, such as how to handle disputes over vacation days in the local country, or how to set and enforce limits on overtime. They may not be able to advise your company on local salary expectations or benefits benchmarks, and they certainly will not be available on the ground to help you recruit new employees and vet those you want to hire.

02 Is there a limit to how long a country allows companies to work through a Global EoR?

Some countries are stricter than others about the time limit they allow for EoR relationships. Germany, for example, allows companies to pay an employee through an EoR for 18 months. After that, a company will have to open an entity and hire the employee directly. The truth is, most EoR solutions are not a long-term option. At some point, whether that's months or years, it makes more sense for the companies to plant roots and open a legal entity of their own, or to walk away from expanding in that specific location.

When they reach a certain threshold of employees, usually in the range of 15-20, the fees they pay on each employee usually grow beyond the financial burden of incorporation costs. At that point, they may also feel that they're ready to expand beyond what EoR can offer, for example, they might want to engage in contracts with partners that require a permanent presence to complete. Until that time though, you want to make sure you can utilize an EoR provider's expertise for as long as you need, and that you won't be caught short by local laws.



In short, you want incorporation to be on your own terms, not forced or accelerated as a result of local laws. The key to planning starts with knowing in advance about any legal limits imposed by the country in question.

03 How does the EoR ensure data privacy and security?

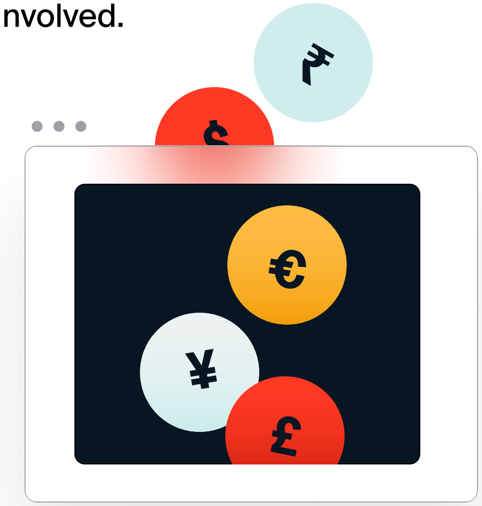
Even before the EU's GDPR regulations came into play, privacy and security were buzzwords in the business world. After all, when it comes to payroll, companies collect and store some of the most sensitive data available about their employees. Before choosing a global EoR, it's essential to learn more about how employee data will be protected. Here's a checklist to get you started:

- Are web transfers, when necessary, completed through the secure HTTPS protocol, with no correspondence sent through standard emails?
- Is access to data limited to the minimum number of stakeholders possible, with the principle of least privilege employed for user access?
- Are files shared via attachments, known to increase data sprawl, or via secure file sharing processes?
- Are there protocols in place for protecting data in transit, as well as at rest?

It's not just a matter of protecting your employees, although of course that's top of every enterprise agenda. The fines for mishandling data can be extremely severe, and yet it doesn't always go without saying that all companies will treat your data privacy with the sensitivity it requires.

04 Which approach does the EoR use for handling IP?

As the employer in the relationship will be the EoR provider, it's important to think about contractual rights such as Intellectual Property, non-compete clauses and non-disclosure agreements, which de-facto will likely belong to the local EoR, not the client themselves. There are many complexities to consider here. In some countries, especially in Europe for example, you cannot mention the clients name in the employment agreement, or say overtly that the IP rights are assigned back to them. Doing this could risk the relationship appearing as employer/employee, or co-employment. Of course, the EoR does not want the contractual rights, it's just a matter of assigning them in an enforceable way. A smart global payroll provider will have flexible solutions that can meet this challenge head-on, and will be happy to discuss this issue openly at the start, and the strategies they use to manage IP rights. In all cases, make sure to choose a partner who can recommend local legal counsel to ensure that your contracts will stand up to scrutiny and enforcement in the locations involved.



05 What pricing model does the EoR use?

When it comes to pricing, there are essentially two approaches a global EoR can choose. It can offer a flat fee for each employee, known as the fixed price model, or it can charge a percentage of the employee's salary. We would always suggest that companies go for option one, as workforce spending is much easier to predict and plan with a fixed price model. When fees are based on how much an employee earns, the numbers are likely to fluctuate from person to person, country to country, and job to job. It becomes difficult to predict how much your company will pay the EoR for their service. On the other hand, if there is a standard fee for each employee, your company will know how much it is paying based on the number of people hired in each location. This becomes even easier when you onboard an aggregator model for EoR, see below.

06 How much flexibility does the EoR show in employment contracts?

Every company has its own policies, and the same is true for every EoR. The question is, what happens when the two sets of policies don't align? How far can the EoR compromise – without violating compliance regulations or local standards – to allow your company to maintain its values and principles? For example, in some cases the EoR may allow you to offer additional benefits such as an enhanced corporate pension scheme, or an end of year bonus, even if it does not already offer these benefits on its own. In reality, there are places where an EoR cannot be flexible, and may need to hold firm because of local laws and regulations, or legalities surrounding how they differentiate and enforce equity between one customer and another.

However, there is a difference between an EoR who is flexible when possible, and others who will insist on sticking to their own standard practices no matter what. Organizations might wrongly believe that they have to do what the EoR wants. After all, they're the ones with the local expertise. However, in some cases, decisions are just preferences by the EoR, not local standards, and there is no reason for companies to accept them, especially if your company culture is at stake.

07 How does the EoR handle Global Equity Management?

It has become commonplace for employers to offer equity as a way of attracting and retaining the best talent. However, equity management and EoR can be a complex issue, regardless of whether you want to offer options, restricted stocks, or performance related shares. You might find that many EoR providers simply refuse to get involved in any equity plans, as they consider the liability too great, and too difficult for them to control.

Your situation will vary greatly depending on the type of company you are, eg: public or private, the countries you are hiring in, and the kind of equity plan you're looking to manage, from Restricted Stock Units (RSUs), Employee Stock Ownership Plans (ESOPs), Employee Stock Purchase Plans (ESPPs), Long-term Incentive Plans (LTIPs) and more.

Ideally, you want to find an EoR provider or Global Payroll solution that can simplify the complexity, handle any eventuality, and work with you across your global equity lifecycle. This means helping you with issues such as registration, grants, vesting and ongoing payslip consideration, as well as pre-tax events, changes in location, and any deductions or additional tax events, as and when they occur.

Understanding the difference between wholly-owned and aggregator models for EoR

One larger issue that it's important to deep-dive into, is whether to choose an EoR provider that is whollyowned, or one that uses the aggregator model. Let's define them both.

Wholly-owned infrastructure

Your EoR provider will open or buy their own local office in each country it serves. Each local office will then be part of a global company, answerable to the main central office of the EoR.

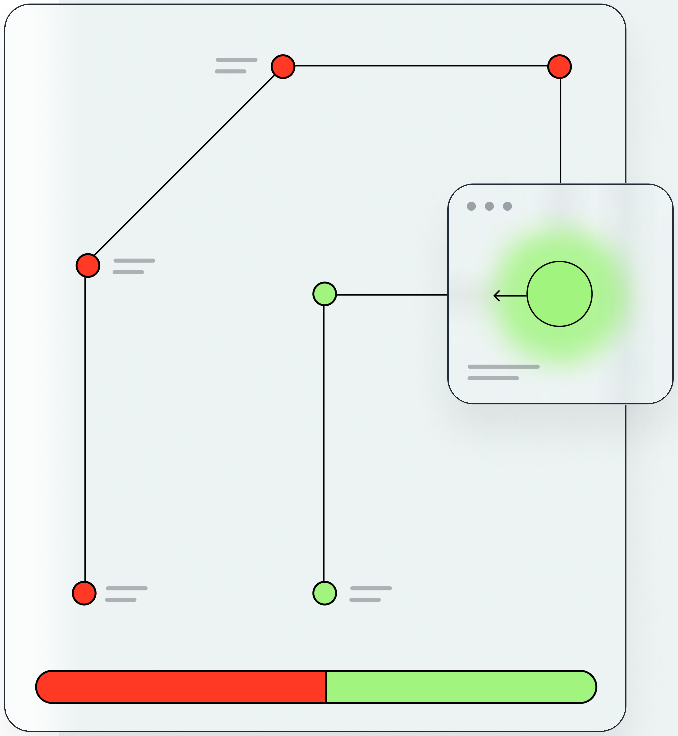
Aggregator model

Your EoR provider will join with an local partner in every country it serves. The client works with the provider, and the provider coordinates on the client's behalf with the ICP.

When you compare the two models – partnership vs full ownership – it's no contest. The aggregator model beats the wholly-owned model in each of the main considerations for choosing an EoR.

Think about the way that Amazon functions in the retail space. It brings together products and vendors, offers full details on all of them, then oversees the experience to guarantee Amazon's high quality of service. An EoR aggregator does the same, bringing together different ICPs, openly sharing information about who they are and the service they provide, then staying with the client every step of the way, to make sure all of their needs are met.

While the wholly-owned model appears to benefit from being part of a single company, in reality, the lack of flexibility, accountability, and transparency make it a liability.



Understanding the difference between wholly-owned and aggregator models for EoR

Aggregator VS Wholly-owned: Head to head

01 Expertise and Quality

Aggregator Model: A global partner carefully vets many potential local partner before choosing the best in class in every location. Local partner are held accountable for the quality of service, and incentivized to meet the highest standards: if the partners underperform, they can be replaced.

Wholly-owned infrastructure: A wholly-owned office cannot be replaced, reducing the incentive to produce top quality work. It is essentially stuck with the infrastructure it has, which is unlikely to be the best in class in any location, and certainly not in every location. Sometimes, the wholly-owned “local” office may not even be located in the country it is serving. In that case, it lacks the local presence to track legislative changes, so compliance is a constant question. It also lacks local knowledge and expertise.

Advantage: Aggregator Model

02 Data Accuracy and Fraud Prevention

Aggregator Model: Workforce data is processed by the local partner but audited by another party, such as the EoR aggregator. This method establishes a two-layer system for ensuring data accuracy on behalf of the client. If the local partner makes an error, it will be spotted in the audit and corrected. The client also has protection against potential fraud committed by the partner.

Wholly-owned infrastructure: A payroll department owned by the company is essentially checking the company's own work and may have a conflict of interest if it finds mistakes by another part of the company. Data lacks integrity if it cannot be independently audited by another party. In addition, the level of protection against fraud disappears entirely.

Advantage: Aggregator Model

03 Flexibility

Aggregator Model: When it comes to EoR service, one size does not fit all. Some local partners are better suited to some clients, not others. An EoR aggregator can leverage multiple partner in one country to find the right fit between client and partner.

Wholly-owned infrastructure: A client cannot choose to work with a different local provider. There is only one choice, and the client has to accept it.

Advantage: Aggregator Model

04 Tailored Service

Aggregator Model: EoR providers may have more than one partner in any region, and can provide a particular expertise, such as tax law, at a client's request

Wholly-owned infrastructure: If it does not have the specific expertise the client needs, the client will have to hire an independent consultant at additional cost.

Advantage: Aggregator Model

05 Advanced IP Protection

Aggregator Model: An aggregator understands the immense value companies place on their intellectual property. Legal clauses in the contracts between aggregators and ICPs ensure that clients retain the IP that belongs to them in any country, despite the differences in IP laws across the world.

Wholly-owned infrastructure: Since it is one company with offices abroad and locally, there are no contracts between them. A client's right to IP is subject to the local laws of the country with no additional protection in place.

Advantage: Aggregator Model

04 Flexibility in Employee Compensation and Benefits

Aggregator Model: A client can choose varied contracts, benefits, and perks in order to attract the best level of talent available. A senior manager can be offered a more attractive compensation package than an entrylevel assistant. Each employee can be compensated at an appropriate and locally competitive level.

Wholly-owned infrastructure: The wholly-owned company generally offers a standard template for all employees, regardless of skill, experience, and responsibility, limiting the level of talent the client can attract and retain.

Advantage: Aggregator Model

	Wholly-Owned Infrastructure	Standard Aggregate Model	
Vetted partners	No	Yes	Yes
Independent Data for Audit	No	Yes	Yes
Flexibility to Choose partner	No	Sometimes	Yes
Tailored service	No	Sometimes	Yes
Extra Layer of Fraud Protection	No	Sometimes	Yes
Full Access to Local Experts	No	No	Yes

	Wholly-Owned Infrastructure	Standard Aggregate Model	
Service Always Carried Out Locally	No	Sometimes	Yes
Legal Protection of Client IP	No	No	Yes
Flat fee with no hidden costs	Sometimes	Sometimes	Yes

Local partners sounds like a win: Why can't I go it alone?

You might be asking yourself, why not just set up relationships with local providers on your own, as and when you need a presence in a new location? We often come across customers who have taken this challenge upon themselves, and they're usually knocking on our door because it's become far more complex than they can handle, or because they're missing out on a lot of the benefits that you can get by consolidating your EoR through one partner solution.

Here are the top benefits, as we see them:

Consistency of operations: Working with one team means that you can have a single point of contact, even if you have employees in 5 or 10 countries around the world. You can get to know your single customer success manager (CSM), strategize with them directly, and help them get to know your company as a whole, not on the basis of the small number of your employees who they deal with in one location.

Ease of work: If you're using 10 different providers in 10 different countries, they may well be in 10 different time zones, or speak multiple languages! With one provider, you are adding a streamlined experience where you speak to one person, who works in your time zone, and who speaks your language, both literally and figuratively. At Papaya Global for example, we have six global offices, which include London, Austin, Melbourne, and Tel Aviv, so we have every time zone covered.

Added layer of due diligence: We discussed above about the conflict of interest that occurs when an EoR is wholly owned. In order to benefit from separate local partnerships, you need an intermediary – an added layer of checks and balances to ensure that you have somewhere to turn in case of fraud, and another set of eyes on your accounts for compliance. Only a consolidated partner makes that happen.

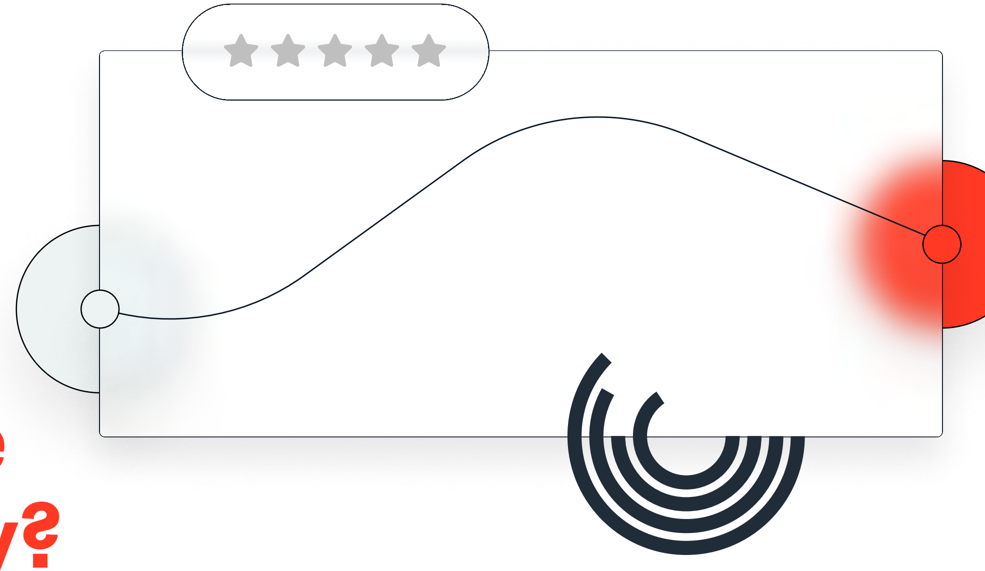
Cost-management: Different local companies will charge according to their unique business model. By consolidating your relationship through one provider, you gain consistency in how you are charged. The best solutions will have one transparent pricing model that is fixed and easy to understand, and will apply to the management of all of your global employees.

Improved future-focus: This can also help you to forecast business costs ahead of time for moving to a new location or adding new employees to the mix. No matter what country your organization finds a great candidate in moving forward, a consolidated EoR partner means you're covered, with none of the initial hassle and reconnaissance.

Economies of scale: Think about how important you are as a customer to a local EoR provider where you have 1 or 2 employees. Frankly, you're a small fish. On the other hand, think about consolidating all your overseas employees into one partner relationship, you suddenly become a lot more important.

Consolidated technology: With multiple global partners, you're forced to use many disparate software solutions, each with its own login details, security measures, and requirements. These will be extremely complicated to manually compare, resulting in additional technology and manual effort for added steps such as reporting or analytics. In some cases, this will be impossible to complete.

Business intelligence: When you're using one interface for your whole payroll experience, you get a single pane of glass into your global workforce. This allows you to take advantage of advanced data management tools such as predictive analytics and trend analysis, supporting effective budgeting or smart workforce management.



How will I know when it's the right time to set up an entity?

Generally speaking, an EoR solution is a short- to medium-term strategy. As your company's global workforce grows, or you gain a foothold in a foreign market, it's important to recognize the signs that it's time to consider opening a legal entity. This is a good thing! It means you've established enough of a presence in the new country to be profitable there, and that you are signalling to potential partners, customers, and employees that you've achieved stability in this region.
Here are three factors that could indicate the time has come to move from EoR to legal entity.

01 A long-term strategy for overseas expansion

Having maximum agility makes sense for a company in the early stages of an overseas operation, especially when it is unsure how large a workforce it will need. But once a strategic decision has been made to build a permanent presence, it becomes cost-effective to open a legal entity.

Having a legal entity also allows a company to engage in better tax planning and apply for grants, subsidies, and incentives in a particular country. Businesses will now be able to truly build their company culture in the new market. When employees feel connected to the long-term goals of their company and feel part of its mission, they are more engaged as workers and more likely to remain with the company, reducing the need to hire and train their replacements, saving costs in the long term.

02 A substantial number of employees

An EoR makes it easy to hire and pay workers, especially when the number is lower than the costs of opening an entity. At a certain point, however, it becomes more cost effective to open an entity to pay workers. It allows the company to eliminate the fees it pays to the EoR, which are typically based on the number of workers, and it lets the company take advantage of better tax rates in some countries.

“At some point, it simply makes more sense to employ rather that outsource employment. This threshold depends on many circumstances, but often comes around 15-20 people in one country. That’s usually the point where companies realize they’ll stay in the country for a longer period or even permanently and that’s where having an entity with payroll becomes more cost effective.

03 Plans to engage in full commerce and contracts

An EoR provides speed, agility, and risk mitigation. That’s ideal for the early stages of a business in a new market. As a business matures and its presence is more established, speed and agility become less important than presence and stability.

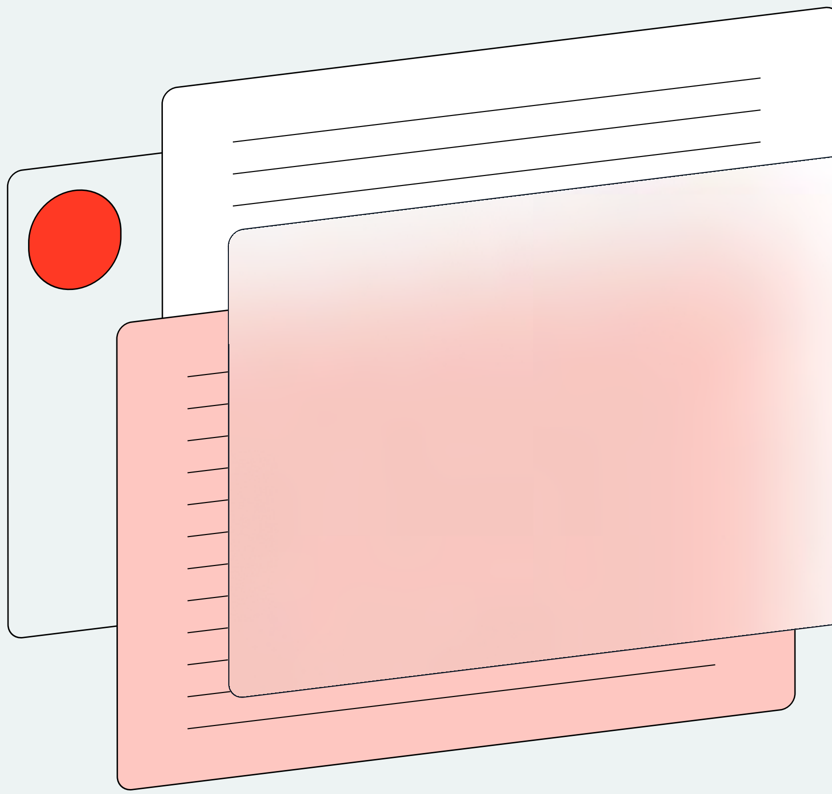
A full legal entity could also open up business opportunities that were unavailable under an EoR relationship, such as engaging in supplier/client contracts through local billing and invoicing. “Clients may be hesitant to do business with a company that’s not actually registered in that country.”

Making the transition from EoR to payroll with Papaya Global

This transition can be complex for organizations to navigate, and this is one of the key ways that Papaya Global differentiates itself against the competition.

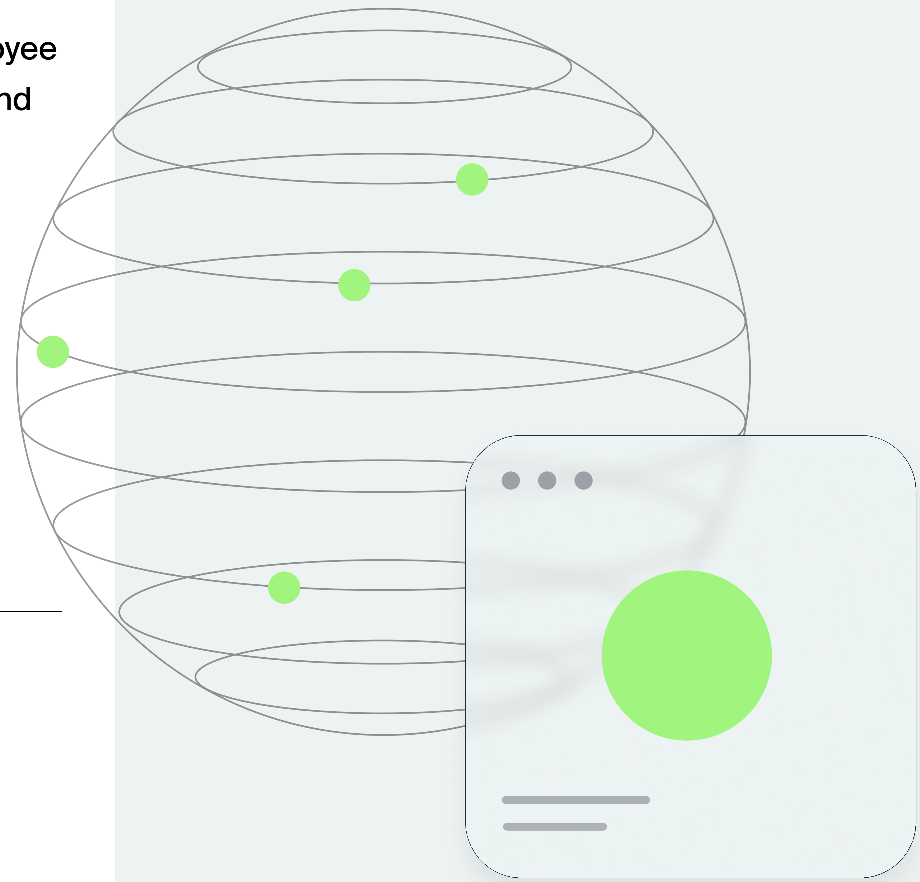
We can support your enterprise in creating a EoR model in a new location where necessary, with global partners in more than 160 countries. We can also provide equal expertise and know-how in incorporating and managing payroll, if and when you’re ready to shift your business model in that direction.

As the only solution for all types of employees and workforces, we can work with you for the long term.



With no specific dog in the race, Papaya is best placed to provide genuine and impartial advice to your business on the right employment model for your needs. Once you've chosen what works for you, we can support a hybrid model of payment processing, the simplest way to handle complex employee payroll, globally. Throughout, you'll have one point of contact to answer all your questions, a single technology solution that integrates with your existing HRIS and ERP systems, provides unparalleled transparency and control, and a unique employee portal for managing and analyzing employee activity, engagement and satisfaction.

At Papaya, we want your company to grow everywhere.



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