PITFALLS TO AVOID WHEN LOCALIZING EXPATRIATES

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Changing financial and strategic priorities, as well as employee-related personal needs, are pushing more organizations to consider localization – that is, adjusting an expatriate's status to that of a local-national employee – when certain scenarios occur. The most common circumstances that would alert human resources to use localization include the following:

- The employee expresses the desire to remain in the assignment location beyond the length of the posting. The family (or the expatriate, if he or she is single) may have no immediately demanding obligations back in the home country and may have built stronger ties than anticipated within their host community – perhaps purchasing a home in the host location, wanting the children to complete their education there, or approaching retirement and wishing to avoid another assignment.
- The end of the assignment draws near, no suitable position is available in the home country, the assignee's talents and experience can be accommodated in the host location, and the assignee is willing to remain on-site.
- The perceived cost inequity between long-term expatriates and local counterparts who do not receive the expatriate "extras" is disruptive to the morale at that worksite.
- Maintaining an employee on a long-term expatriate package can be extremely costly for the firm, and the organization is concerned about cost containment and reduction.

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It may also happen that the organization needs the expatriate's skills and experience to remain in the assignment location for an extended period. For example, perhaps the opening of a particularly difficult operation in the host country is taking longer than originally estimated, or the repatriation of an assignee would leave a detrimental skills gap in the host location that cannot be readily filled with a local-national employee. When the decision to extend the assignment comes from the employer, localization is more problematic and may involve some negotiation to enhance the local package.

As simple as the concept of localization may be, actual implementation poses a whole host of complex issues. During the process, an employer might face two particularly difficult issues: having an inadequate policy (or none) and creating the right pay package. Whether they successfully transition the assignee's status depends on how they address both matters.

TROUBLE SPOT #1: LACKING A POLICY

Localizing an expatriate may prove more difficult than need be due to a number of factors that tend to inhibit the process, such as a lack of strategy or plan to effectively staff the host-country operation and/or a lack of policy or even informal guidelines to implement the change. In most cases, the number of employees to be localized represents a small minority of the company's expatriate population, so the company has not spent much time or effort in addressing their situation.

The resulting scenario is similar to what happens when companies initially send their first expatriates abroad: Negotiations on a case-by-case basis are the norm. Unfortunately, without any structure or policy, unreasonable expectations often exist between managers and expatriates. The lack of a policy and the resulting negotiations can also lead to inequity among localized assignees, forcing some companies to reconsider their situation. According to ORC's *2006 Worldwide Survey of International Assignment Policies and Practices*, a localization policy is one of the top five areas currently under review by 30 percent of Europe/Middle East-based firms, 38 percent based in the Americas, 47 percent in Asia-Pacific, and only 4 percent of Japanese companies.

At present, survey respondents reported that 68 percent worldwide have yet to implement a localization policy. Only 21 percent have a formal policy, and 11 percent have an informal one. For those organizations that have implemented some form of localization policy, only 17 percent follow it strictly; 77 percent handle such occurrences on a case-by-case basis. Apparently, most organizations do not have a policy for localizing expatriates – and even when they do, many do not follow it, or they are willing to make exceptions to all or most of the rules. Basing localization decisions on such a loose framework enhances the potential for employee relations problems down the road if the employer does not follow a consistent and equitable approach.

TROUBLE SPOT # 2: CREATING A PAY PACKAGE

When an organization is localizing an expatriate, difficulty often revolves around retirement and social security, income taxes, housing, and dependent education. A common pitfall involves picking the best compensation elements from both the local-national and expatriate plans, often resulting in a package that does not seem to please any of the parties and possibly resulting in high costs. So, how can companies successfully address this issue?

For one thing, employers should recognize that the underlying rationale for localizing the individual will have an impact on the type of remuneration package offered. When an individual asks to remain in the assignment location, the employer need not be as generous with its pay package. However, when a business decision drives the need for localization, the firm has less leverage for negotiation.

The home-and-host country combination also affects the employer's ability to create a pay package that is acceptable to all parties. Localizing an expatriate originating from a developed country to a lesser-developed country can be extremely challenging, as assignees often have concerns about the relative cost and standard of living in the host location – and the new package may represent too great a reduction. (Localizing an expatriate to a more developed country, as expected, is often easier to implement.)

Timing is another factor. Localization rarely occurs during the first three years of an assignment (see chart 1, "Trends in Localization Timing"). And when it comes to reducing an expatriate's remuneration, 6 percent of the respondents to ORC's *2006 Worldwide Survey* do so after 3 years, 12 percent reduce pay after five years, and 12 percent do so on a case-by-case basis. Fifty percent, however, do not reduce pay regardless of assignment length. (See chart 2, "When Employers Reduce the Pay Package.")

Reducing an expatriate's pay package takes different forms. Those assignees placed on a pure host-based compensation package conform to the assignment-location salary structure and receive pay in local currency. Consequently, an expatriate and a local-national employee who are doing similar work receive comparable salaries. Although such plans are intended to eliminate cost equalizers and premiums, some companies still provide for foreign housing, tax treatment, and certain other elements (e.g., home leave) on an expatriate basis if the assignee's unique circumstances warrant it. However, this type of thinking can result in a very generous total compensation package — causing difficulties if the organization is trying to contain costs.

To help the assignee ease into the loss of any "extras" that are being eliminated, some organizations consider phasing in the new package rather than implementing it immediately – or even offer a "buy out" of some kind. For example, many employers phase out the cost-of-living adjustment over two or three years, or stop them immediately, accompanying the cessation with a lump sum payout. If the employer follows tax equalization, it usually phases out that practice, along with any assistance for tax preparation. For those items that are continued for some period, the employer should inform the individual of the end date and allow sufficient time for the employee to adjust to the change in finances.

CHART 1

Trends in Localization Timing

AFTER HOW MANY YEARS ON ASSIGNMENT DOES YOUR COMPANY LOCALIZE ASSIGNEES?

WORLDWIDE RESPONDENTS

1-3 YEARS	3-5 YEARS	6-10 YEARS	ASSIGNMENT REGION
5 %	49 %	46 %	Asia (excluding Japan)
7	54	39	Europe
9	54	37	North America
7	49	44	Central or South America
6	49	45	Japan
6	47	46	Africa
6	47	46	Middle East

Source: ORC Worldwide's 2006 Worldwide Survey of International Assignment Policies and Practices

CHART 2

When Employers Reduce the Pay Package

DOES YOUR COMPANY REDUCE THE EXPATRIATE REMUNERATION PACKAGE AFTER A CERTAIN PERIOD AT THE ASSIGNMENT LOCATION?

ASIA PACIFIC	EUROPE/ MIDDLE EAST	JAPAN	THE AMERICAS	WORLDWIDE	
3%	11%	0%	6%	6%	Yes, after three years at assignment location
7	20	2	14	12	Yes, after five years at assignment location
0	1	1	0	0	Yes, after eight years at assignment location
10	11	3 1	7	12	Yes, on a case-by-case basis
3	4	4	5	4	Yes, other than above
51	42	85	40	50	No
25	11	6	18	14	Situation has not occurred

Source: ORC Worldwide's *2006 Worldwide Survey of International Assignment Policies and Practices*

AVOID THE OBVIOUS PITFALLS

Faced with a decision to localize an expatriate after a certain period, employers must carefully weigh the particulars of their circumstances, the organizational and specific assignment objectives, budget restrictions or flexibility, corporate culture, and human resources policies. What works for one organization when localizing expatriates often will not work for another firm – or not as successfully.

An appropriate compensation approach and policy for localizing expatriates should reinforce the company's overall business and specific operational needs, as well as enhance the career development of assignees. Having a formal policy and compensation framework in place (or, at least, informal guidelines) and communicating them clearly are essential to avoid unnecessary morale and inequity issues.