

OECD Secretariat Analysis of Tax Treaties and the Impact of the COVID-19 Crisis

Newsletter by PwC Georgia Tax Team

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On 3 April 2020, at the request of concerned countries, the OECD Secretariat released a guidance on tax issues arising from the cross-border workers affected by the COVID-19 crisis. The focus of the guidance is to address the concerns of the businesses that the restrictions on travel or movement or quarantine requirements as a result of the COVID-19 pandemic would change corporate residence, create permanent establishments (PEs), or result in other undesirable tax consequences.

Based on an analysis of existing treaties, the Secretariat stated that generally working from home or concluding contracts from an employee/agent's home should not be sufficient to create a PE, and that a temporary halt in work at a construction site should not dissolve a PE. Neither should the COVID-19 affect treaty residency of the enterprises due to relocation of the chief executives or residency of the employees due to moving to another country during the crisis period.

The analysis also explains that in most instances the receipt of subsidized income payments by temporarily displaced employees should be attributable to the country they used to work before the COVID-19. Although, where the source country has the right to tax such income, based on the double tax treaty a residency country should relieve it either through granting an exemption or giving the right for a foreign tax credit.

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Issue №1: Concerns related to the creation of permanent establishments

Issue:

Some businesses are concerned that due to COVID-19 situation their employees are stranded in a country that is not their place of regular work and as a result, the working from their homes may create a PE of the employer in that country. Besides, the question is also raised whether temporary working of the individual from the home may create a dependent agent PE for his/her non-resident employer. Another question relates to construction site PE and specifically, whether the

temporary interruption of construction works may affect the PE position and whether such interruption period should be counted for the PE threshold purposes.

Position of the OECD Secretariat:

The guidance elaborates on the above issues and observes that, it is unlikely that the COVID-19 situation should create any changes to a PE determination. The logic for such conclusions is explained as follows:

Home office – It is less likely that key characteristics attributable to PE, that is a certain degree of permanency and having a place at the disposal of the foreign entity, would be satisfied in the given situation. During the COVID-19 crisis, individuals who stay at home to work remotely are typically doing so as a result of government directives: it is force majeure, not an enterprise's requirement. Respectively, home office should not create a PE for the business/employer, either because such activity lacks a sufficient degree of permanency or continuity or because the employer would not have access or control on the home office, and hence, it will not be at its disposal.

Agency PE – When a person is working at home in a country for a short period because of force majeure and/or government directives, it is unlikely to be regarded that he/she is working in a habitual way. Respectively, such temporary activities should not create an agency PE of a non-resident employer.

Construction site PE – Generally, the double tax treaties set time threshold when a construction site becomes a PE. According to the commentaries to OECD Model Convention, a site should not be regarded as ceasing to exist when work is temporarily discontinued (temporary interruptions should be included in determining the duration of a site). Respectively, the duration of a temporary interruption during the crisis period should however be considered in the life of a site and therefore will affect the determination whether a construction site constitutes a PE.

effective management" of a company as a result of a relocation, or inability to travel, of chief executive officers or other senior executives.

Position of the OECD Secretariat:

According to the guidance it is unlikely that the COVID-19 situation will create any changes to an entity's residence status under a tax treaty. A temporary change in location of the chief executive officers and other senior executives is an extraordinary because of pandemic and other quarantine restrictions and such change of location should not trigger a change in residency. Nevertheless, if due to domestic legislation, a dual residency issue appears, it would be resolved under tie-breaker rules set in the respective double tax treaty.

Issue №2: Concerns related to the residence status of a company (place of effective management)

Issue:

The second issue relates to the concerns related to the residence status of a company, since the COVID-19 crisis may lead to a potential change in the "place of

Issue №3: Concerns related to cross-border workers

Issue:

Another question relates to the taxation of cross-border workers' salaries subsidized by the government. Specifically, in some countries the government proposed to provide wage subsidies to employers in order to keep the workers on the payroll during the COVID-19 crisis. Although, in certain cases the workers could be residents of one country but commuting to another country to execute their duties in a normal course of their employment. The questions raised about the distribution of taxing rights between the countries with respect to subsidized salaries for such cross-border employees whereas they are restricted to exercise their employment duties and stalled in their residency country.

Position of the OECD Secretariat

The OECD Secretariat observes that such payment stands close to the termination payments discussed in the paragraph 2.6 of the commentary on Article 15 of the OECD Model Convention and should be attributable to the country where the employee would otherwise worked should the crisis did not appear. In most circumstances, this will be the place the person used to work before the COVID-19 crisis.

In turn, where the source country has a taxing right, the residence country must relieve double taxation under the relevant tax treaty, either by exempting the income or by taxing it and giving a credit for the source country tax.

Issue №4: Concerns related to a change to the residence status of individuals

Issue:

The final issue addressed by the OECD Secretariat relates to unforeseen place changes of the individuals that might affect their tax residency status.

Position of the OECD Secretariat:

The OECD Secretariat states that it is unlikely that the COVID-19 situation will affect the treaty residence position of the individuals.

It provides two possible scenarios where individual's domestic residence status might change due to COVID-19 crisis:

1. A person is temporarily away from home (on holidays, on work for few weeks) and gets stranded in the host country due to COVID-19 situation where he/she acquires domestic law residence there.
2. An individual was working in a country where has attained residence status, but temporarily returns to his/her "previous home country" due to COVID-19. They may either never have lost their status of resident in their previous home country or they may regain it on their return.

However, the Secretariat defines that in both scenarios, if a tax treaty is available, the treaty tie-breaker rules should solve the issue and keep the person resident of the country he/she was before the COVID-19 crisis.

Moreover, the Secretariat also observes that because the COVID-19 crisis is a period of major changes and exceptional circumstances, in the short term tax administrations and competent authorities should have to consider a more normal period of time when assessing a person's resident status.

Source: https://read.oecd-ilibrary.org/view/?ref=127_127237-vsdagpp2t3&title=OECD-Secretariat-analysis-of-tax-treaties-and-the-impact-of-the-COVID-19-Crisis

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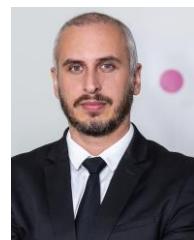
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