COVID-19 Tax Issues – the OECD Checklist

INTRODUCTION

1. COVID-19 has posed huge challenges to the global community. Normal patterns of work have been upended, careful plans made for tax purposes around, for example, the location of workers and the physical location of board meetings have, of necessity, been abandoned. Whilst, as one would hope, tax authorities are taking a sympathetic approach, there does not appear to be a blanket offer that all of the difficulties thrown up by COVID-19 will be ignored for tax purposes and the slate wiped clean after the pandemic is over, so any sympathy is tainted with the potential for rigour and tax advisers must ensure their clients have a clear view of the specific tax risks presented by the crisis and how to manage them.

OECD SECRETARIAT'S ANALYSIS

2. Earlier this month the OECD Secretariat issued an analysis of the interaction between the ongoing COVID-19 pandemic and the treatment of taxpayers under tax treaties (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). In particular the analysis looks to address concerns that lockdown measures implemented by governments across the world will lead to enterprises and/or people becoming taxable in a different jurisdiction from the one in which they normally pay tax.

3. In short, the concerns identified are:

   (1) that employees may create a permanent establishment (**"PE"**) when working from home in a different jurisdiction from the one in which they usually work;

   (2) that the "place of effective management" and therefore tax residence of a company will shift;

   (3) that an individual's tax residency status may alter; and

   (4) how to properly tax government subsidised payments for cross-border employees.

4. The underlying tenor of the OECD's paper is that as the COVID-19 pandemic and the resulting measures adopted by governments are temporary and extraordinary they will

generally not affect the treatment of people and enterprises by tax treaties. However, this analysis must be read with the following caveats in mind:

(1) it is not clear when the world will be free of some form of restriction on travel and movement by governments, it may be some time before government policy returns to normal.

(2) many commentators are speculating that patterns of work will not return to normal even after governments lift the current restrictions.

(3) as ever, the domestic law of relevant jurisdictions will be vital to consider (for example, when determining an individual's tax residence) along with any measures or guidance that they have produced to deal with these particular problems;

(4) the approaches adopted to restricting the spread of COVID-19 are not consistent across nations (or even the European Union), and whether a particular change in working or living circumstances are government mandated or an individual choice may be relevant; and

(5) as ever, the particular facts of any given circumstances will need close analysis.

5. The analysis provided by the OECD is, however, comforting in that it reminds taxing authorities that in dealing with issues brought up by COVID-19, they ought to recognise that the COVID-19 circumstances are exceptional and that they should adopt a broad view of the facts when addressing the issues set out below.

Permanent Establishments

6. Before the COVID-19 pandemic struck there were various instances of individuals who lived in one country (Country A) and worked in another (Country B). For example, an individual may have a family in France but normally spend Monday to Friday working in an office in Britain, or *vice versa*. With travel bans instituted by various governments, many of these people have been forced to work from home rather than cross a border to reach the office. In such circumstances the issue arises as to whether that employee creates a PE in the country in which the home office is located (Country A), and so exposes the employer to tax in that country on profits attributable to the PE.

7. The OECD Secretariat's analysis is that where an employee is using a home office in such circumstances, it is unlikely that a PE will be created for tax treaty purposes. The OECD notes that as the employee is working from home as a result of extraordinary measures instituted by governments, it is unlikely the employee's home office will have the sufficient degree of permanency required to create a PE and it is unlikely that the employer will have sufficient access or control over the home office. The company would not have relevant foreign premises at its disposal.

8. The OECD sensibly predicates its advice on the assumption that this form of work does not become the norm over time. It also, in part, supports its analysis by noting that the employer will still be providing an office which, in normal circumstances, would be available to its employees.

9. However, whether or not a PE has been created will require a factual enquiry into the specific circumstances at hand. On top of the normal considerations for whether a PE has been created the following factors may be relevant:

   (1) whether the employer has been able to maintain an office in a different country which the employee could, but for the COVID-19 restrictions, use. If the company has shut the office to save money, it may suggest a greater degree of permanency in the home office arrangement;

   (2) whether the company is planning on moving employees to working from home on a more permanent basis after the COVID-19 restrictions are lifted;

   (3) the length of time the employee has been working from home;

   (4) whether the employee is working from home as a result of government policy or as a result of a decision taken by the employer;

   (5) whether the employer has installed equipment into the employee's house so that s/he can work from home. If the employer has installed computers, video conferencing hardware, or a secure internet connection, that may support an argument that a PE has been created;

   (6) the proportion of the employer's workforce now working from home, and operating from a different jurisdiction.

10. In determining whether a dependent agent PE is established by an employee working from home and concluding contracts on behalf of the his/her employee businesses will require consideration of issues similar to those set out above. However, as under the OECD Model Convention such a PE may be created when the agent habitually concludes contracts on behalf of the employer, questions of how long the situation lasts and whether it becomes a new normal will be particularly pertinent.

11. The opinion of the OECD Secretariat is helpful, but the specific facts pertaining to individual taxpayers, the approach of different jurisdictions, and the duration and any long-lasting effects of the pandemic to working conventions will require close analysis.

Corporate Residence

12. Another area of potential concern is that of corporate residence. With people confined to their houses or to a particular country, it may no longer be possible for a company to be managed or controlled from the country in which it is normally resident.

13. Insofar as tax treaties are concerned the OECD Secretariat considers that the COVID-19 situation is unlikely to affect the residency of companies. As the Secretariat's analysis correctly points out the matter of company residence is usually an issue of domestic law and companies are rarely resident in more than one jurisdiction. Further and in any event, in accordance with the commentary, where the "tie-breaker" provisions in the OECD Model Conventions apply they are primarily concerned with where the control and management of a company "usually" or "ordinarily" takes place. Provided the measures taken to continue the management of a company remotely can be described as extraordinary or unusual, then one would not expect them to alter the residence of a company.

14. However, where a Mutual Agreement Procedure (**"MAP"**) is in place between countries the position is perhaps more uncertain as the outcome will depend upon the approach of the relevant tax authorities. The OECD analysis in relation to tax treaties has provided helpful guidance by suggesting that factors such as where the chief executive officers usually carry out their duties ought to be relevant, but it may be that the relevant tax authorities take a different view and it is that view which will be determinative under MAP.

15. Further and in any event, the underlying assumption of the Secretariat's analysis is that the measures required to combat COVID-19 are indeed temporary and do not result in longer-lasting changes either to the way in which a particular company conducts its business or in which business as a whole is conducted. If the measures last for longer than expected then more companies may have to start to rely on the "tie-breaker" provisions in tax treaties or MAP as they may become dual-resident over time. As such, where companies have made temporary adjustments to their management (with, for example, executives staying in their home jurisdiction and attending meetings by video link rather than in person) they would do well to keep clear evidence of the fact that it is only a temporary measure and that once restrictions are relaxed they will return to their usual practice.

Individual's residency status

16. Individuals will need to consider whether their tax residency will be altered as a result of COVID-19 restrictions. There are two key situations in which this might occur:

    (1) a person who is out of their country of residence when lockdown provisions are instituted becomes trapped in a different country; and

    (2) a person returns to a country in which they are no longer resident in order to be close to family and/or friends.

17. The particular circumstances will of course be highly factually dependent, including a consideration of the laws in the relevant jurisdictions. However, the OECD analysis does provide some helpful guidance on the position under tax treaties.

18. The starting point for determining an individual's residence is domestic law. If the individual only meets the residency requirements of one jurisdiction then that is the end of the matter. However, where an individual is potentially resident in multiple jurisdictions, then the tie-breaker rules in Art.4 of the OECD Model Convention are engaged, and employ a hierarchy of tests to determine where the individual is resident.

19. The OECD's analysis suggests that the temporary measures imposed by governments in response to COVID-19 are unlikely to lead to individuals having a change in residency. Whilst they are broadly correct in this approach, it is likely that more individuals will have to rely on the tie-breakers in Art.4 of the OECD Model Convention in order to determine their residence (as they pass the time thresholds for

being resident in a different jurisdiction). The hierarchy of the tests is summarised below:

(1) does the individual have a permanent residence in either or both jurisdictions?

(2) with which country does the individual have closer personal and economic relations?

(3) in which country is the individual's habitual abode?

(4) what is the individual's nationality?

20. For the individual in the first scenario (i.e. trapped in a foreign country), it is perhaps unlikely that the answers to these tie breakers will shift to cause them to be resident in that country. For the individual in the second scenario however (i.e. returned home to be close to family and/or friends) it may well be that as the crisis persists the answers to these questions also change and will require careful monitoring. For example, such an individual may lose economic connections with the country from which they returned, having a permanent residence in the original country. As ever the factual circumstances will be highly determinative, and once an individual crosses the time threshold for residency in another jurisdiction they must seriously consider the answers to the tie-breaker questions set out above.

Cross-border workers

21. One final area of the OECD's analysis that is worth briefly highlighting is that concerning the tax treatment of government subsidies paid to cross-border workers. Many governments have taken steps to subsidise the keeping of an employee on a company's payroll during the COVID-19 pandemic. In circumstances in which the employee lives in a different country from that in which they used to work a question arises as to which country has the right to tax the monies received by the individual under such a scheme.

22. The OECD analysis typifies these payments as most closely resembling termination payments and that as such they should be attributable under Art.15 of the OECD Model Convention to the place where the employee would otherwise have worked, which in most cases will be the place they used to work before the crisis.

23. This is, however, a complex and factually dependent matter mainly outside the scope of this article which is simply highlighted here. Amongst other things it will be necessary to consider the exact nature of the payment, whether the employee has ceased to work for their employer, and whether where the employee exercises their employment changes. The OECD has promised to work with countries to mitigate unplanned tax implications of the COVID-19 pandemic and this will be an area of particular interest.

HMRC'S APPROACH

24. HMRC has issued guidance pertaining to the issues highlighted above and in the OECD analysis. Whilst this will be helpful for many who are concerned about what impact the COVID-19 pandemic could have on their tax status in relation to the UK, the guidance is very generalised and so, as cautioned above, a thorough factual analysis of the circumstances will be needed. In addition, it should be borne in mind that HMRC's guidance is just that and not law, although it demonstrates how HMRC will approach these questions in the current situation.

Individual's residency status

25. Under the normal statutory residence test for individuals, an individual will be regarded as being within the UK – and therefore such a day will count towards their 'day-count' - if they are here at midnight. There are exceptions to this however, most importantly for these purposes that of "exceptional circumstances". HMRC have released guidance as to when the exceptional circumstances condition would be regarded as having been met during the COVID-19 pandemic, meaning those days will not be counted for the statutory residence test. The guidance makes clear that in each case it is a question of the specific facts and circumstances, but states (at RDRM11005) that the following will be regarded as 'exceptional circumstances':

- if an individual is quarantined or advised by a health professional or public health guidance to self-isolate in the UK as a result of the virus;
- if an individual finds themselves advised by the official Government advice not to travel from the UK as a result of the virus;
- if an individual is unable to leave to leave the UK as a result of the closure of international borders;

- if an individual is asked by their employer to return to the UK temporarily as a result of the virus.

26. Whilst this guidance will apply to many who are now spending additional time within the UK, it does not address, for instance, individuals who are in the UK to care for family members etc. as a result of the virus. Such would have to be covered by the normal 'exceptional circumstances' rules, under which there is provision for caring for a spouse, civil partner, person they are living with or dependent child. Further, this guidance is subject to the normal restrictions relating to exceptional circumstances, and advisers should be careful to check whether clients will ultimately be impacted by the statutory residence test. For example, the 'exceptional circumstances' exception only applies to certain aspects of the statutory residence test, and not others. Further, the total number of days which can be ignored owing to exceptional circumstances is 60 days. Whether an individual will have days to take into account as a result of the virus could therefore depend on when particular travel restrictions are lifted, bearing in mind the statutory residence test applies by reference to tax years, and the current tax year 2020/21 started on 6 April 2020 and thus during the pandemic.

27. In addition to this guidance from HMRC, the Chancellor has made it clear, in a letter to the Chair of the Treasury Committee dated 9 April 2020 that the statutory residence test will be temporarily amended as it relates to foreign key workers. Any foreign key workers who spend time in the UK between 1 March 2020 and 1 June 2020 and are involved in "COVID-19 related activities" will not have that time taken into account for the purposes of the statutory residence test. There will be strict qualification criteria to be a key worker that comes within this, to minimise the risk of abuse. However, at the time of writing these criteria have not been set out. This change will be included within Finance Bill 2020, with effect from 1 March 2020.

Corporate residence

28. In relation to corporate residence, HMRC has also issued guidance at INTM120185 and INTM261010. Notably, this references HMRC being "*very sympathetic to the disruption that is being endured*." HMRC's stance is that the existing legislation and guidance is sufficient to deal with board meetings taking place, or decisions being made within the UK during the COVID-19 pandemic. This is on the basis that HMRC will take a 'holistic' view of all the facts and circumstances, and so a company will not

necessarily become tax resident in the UK where such changes in business activities are necessary. In particular, HMRC point to their guidance (at INTM120140, 120150 and 120160, including examples) relating to when they would not normally challenge a company's view on its residence.

29. Advisers should check whether the particular changes a client has had to make to its business could result in the central management and control being located within the UK. If so, they could look into actions such as temporarily changing the articles to amend the structure or timing of board meetings, for example, or indeed amending the board composition or voting rights. It is also worth checking whether the company would also be regarded as tax resident in another jurisdiction, in which case any tie-breaker provision within a double tax agreement, as discussed above, would need to be applied to determine residence.

30. In relation to the question of whether companies could inadvertently establish PEs in the UK during the current crisis, HMRC again reiterate their sympathy and that they consider the current legislation and guidance provides sufficient flexibility to deal with this. HMRC states that, again, it is a question of fact and degree whether there is a habitual conclusion of contracts in the UK, and that they do not consider a non-resident company will automatically have a taxable presence after a short period of time as a degree of permanence is required. HMRC also point out that even if a UK PE is created, this does not in itself mean a significant amount of profits would be taxable in the UK, which would of course depend on the particular facts of any given case.

31. This guidance might not provide much comfort for clients concerned about a PE being created, and advisers should review the position carefully in light of the rules and any relevant double tax agreement. Where it is not clear if a PE will be created, it would likely be worth contacting HMRC to clarify the position and see what impact their sympathy has.

Summary and practicalities

32. HMRC's issued guidance on tax residence related issues during the COVID-19 pandemic should provide some comfort to potentially affected taxpayers, particularly individuals. However, as it is in very generalised terms and would have questionable enforceability, it is likely there will be situations where the position is still not clear, or

indeed where the tax residence shifts as a result of actions taken in response to the crisis. Advisers should therefore review the facts of any case carefully.

33. Whilst contemporaneous records and evidence are always important, they are potentially more so now in case HMRC do seek to dispute the tax residence. For example, meeting minutes could indicate that they had to be held remotely due to the travel restrictions or lockdown measures in place. Documents should also be maintained to ensure any question of establishing a PE is being monitored. As suggested above, where a company is concerned about its central management and control being in the UK, it should look into whether any practical changes can be made to the manner in which business is carried out, so that important meetings and decisions are not taken, inadvertently, within the UK to an extent that it could change the tax residence status.

34. For how these residence issues have been dealt with by other jurisdictions, and other international aspects, see the excellent article by Ben Jones and Kunal Nathwani, "*Where do I lay my hat?*" (Taxation, 9 April 2020).

CONCLUSION

35. It cannot be assumed that tax authorities will simply ignore everything that happened during the pandemic and, especially where large amounts are at stake or there are ongoing disputes, it may well be that such authorities look to enforce the rules with a degree of rigour. Amidst all of the noise, advisers should not lose sight of key issues such as residence and place of management most likely to be affected by the pandemic upheaval. The review of these issues needs to be in the context of a holistic review of the business as a whole, any cross-border tax issues and the impact of both domestic and international COVID-19 tax policies and guidance.

Francis Fitzpatrick QC, Sarah Black and Edward Hellier

11 New Square

29 April 2020