

OECD Secretariat issues updated guidance on tax treaties and the impact of COVID-19 pandemic

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Executive summary

On 21 January 2021, the Organisation for Economic Co-operation and Development (OECD) published on its website an *Updated guidance on tax treaties and the impact of the COVID-19 pandemic* (the [guidance](#)). This guidance revisits the guidance published on 3 April 2020¹ by the OECD Secretariat.

The updated guidance provides an analysis of some of the treaty-related issues that may arise due to the COVID-19 pandemic and intends to provide more tax certainty to taxpayers. The guidance represents the OECD Secretariat's views on the interpretation of the provisions of tax treaties (i.e., each jurisdiction may adopt its own guidance to provide tax certainty to taxpayers). However, the document indicates that the guidance reflects the general approach of jurisdictions and illustrates how some jurisdictions have addressed the impact of COVID-19 on the tax situations of individuals and employers.

The guidance addresses the following issues:

- i. Permanent establishments
- ii. Residence status of companies (based on place of effective management) and individuals
- iii. Treatment of employment income

This updated version of the guidance considers some additional fact patterns not addressed in detail in the April 2020 guidance, examines whether the analysis and the conclusions outlined in the April 2020 guidance continue to apply where the circumstances persist for a significant period, and contains references to country practice and guidance during the COVID-19 pandemic.

Detailed discussion

Background

The OECD has published on its [website](#) diverse materials related to different focus areas in response to the COVID-19 crisis, including materials on both tax administration and tax policy responses.

On 3 April 2020, the OECD published on its website an *OECD Secretariat Analysis of Tax Treaties and the Impact of the COVID-19 Crisis*. The analysis provided guidance on the tax implications of the dislocation of cross-border workers due to the COVID-19 pandemic, considering the relevant tax treaty provisions.

On 18 December 2020, the OECD released a report containing guidance on the transfer pricing implications of the COVID-19 pandemic. The Report focuses on how the arm's-length principle and the OECD Transfer Pricing Guidelines apply to issues that may arise or be exacerbated in the context of the COVID-19 pandemic.

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

On 21 January 2021, the OECD published updated guidance considering additional fact patterns not addressed in detail in the April 2020 guidance. The analysis in the guidance is based on the OECD Model Tax Convention (OECD Model), but also includes one reference to the United Nations Model Tax Convention. The guidance is intended to provide more certainty to taxpayers during this exceptional period of the COVID-19 pandemic.

The guidance does not represent the official views of the OECD member countries and includes an acknowledgement that jurisdictions may adopt their own guidance to provide tax certainty to taxpayers. However, the guidance reflects the general approach of jurisdictions and illustrates how some jurisdictions have addressed the impact of COVID-19 pandemic on certain the tax situations. In addition, it should

be noted that, in contrast to the April 2020 guidance, the updated guidance includes a footnote indicating that it was discussed in OECD Working Party 1 in its Inclusive Framework configuration, which supports its publication.

The updated guidance further specifies that it is relevant only to circumstances arising during the COVID-19 pandemic when public health measures are in effect. It indicates that it is aimed at avoiding instances of double taxation and cannot be relied on to create double non-taxation.

Concerns related to the creation of permanent establishments

The updated guidance covers the same type of permanent establishment (PE) issues covered in the April 2020 guidance. The overall conclusions remain unchanged, but there are a few differences in comparison to the April 2020 guidance.

► **Home office PE:** Consistent with the April 2020 guidance, the updated guidance confirms that individuals teleworking from home (i.e., a home office) as a result of a public health measure imposed or recommended by at least one of the governments of the jurisdictions involved would not create a fixed place of business PE for the business/employer. However, the updated guidance further elaborates on the conclusion by noting that individuals who stay at home to work remotely during the pandemic are typically doing so as a result of public health measures. Working from home as a result of public health measures is an extraordinary event and it is not a requirement of the employer. Therefore, considering the extraordinary nature of the COVID-19 pandemic, working from home would not create a PE for the business/employer, either because such activity lacks a sufficient degree of permanency or continuity or because the home office is not at the disposal of the enterprise. In this regard, the updated guidance further notes that the employer still provides an office that would be available to the employee absent the public health measures. This analysis applies whether the temporary work location is the individual's home or a temporary dwelling in a jurisdiction that is not his or her primary place of residence.

The updated guidance also states that if the individual keeps working from home after the public health measures are not applicable anymore, the home office may be considered to have a certain degree of permanence. However, this change alone will not necessarily result in the home office giving rise to a fixed place of business PE. After such a permanent change, a further examination of the facts and

circumstances would be required to determine whether the home office would then be considered to be at the disposal of the enterprise.

- ▶ **Agency PE:** Similar to the April 2020 guidance, the updated guidance concludes that an employee's or agent's working from home during the pandemic is unlikely to constitute an agency PE if the employee/agent does not habitually conclude contracts on behalf of the enterprise. The employee's or agent's activity should not be regarded as "habitual" if they have exceptionally begun working from home as a result of a public health measure imposed or recommended by the government and provided the individual does not continue those activities after the public health measures cease to apply. The updated guidance also indicates that a different approach may be appropriate, if the employee was habitually concluding contracts on behalf of the enterprise in their home jurisdiction before the COVID-19 pandemic.

In contrast with the earlier guidance, the updated guidance provides that if the employee keeps working from home after public measures are not applicable anymore and continues to habitually conclude contracts on behalf of the enterprise, it would be more likely that the employee would create an agency PE. In that respect, the updated guidance provides that the same factors considered in paragraphs 28 to 30 of the commentary on Article 5 of the OECD Model are relevant for the analysis. These paragraphs note, for example, that experience has shown that PEs normally have not been considered to exist in situations where a business had been carried on in a country through a place of business that was maintained for less than six months. Further, the paragraphs indicate that the recurrent nature of the business operations is important to an assessment of the degree of permanency and also whether the activity is wholly carried on in that country.

- ▶ **Construction site PE:** In line with the April 2020 guidance, the updated guidance concludes that a construction site PE would not be regarded as ceasing to exist when work on the site is temporarily interrupted. However, jurisdictions may consider, in light of the extraordinary circumstances of the COVID-19 pandemic and based on the facts and circumstances, that certain periods where operations are prevented because of a public health measure imposed or recommended by the government where the site is located to reduce the spread of the COVID-19 virus constitute a type of interruption that should be excluded from the calculation of time thresholds for construction site PEs.

Therefore, some jurisdictions may include COVID-related interruptions when calculating the time threshold for the construction PE, while other jurisdictions may exclude those interruptions, which can lead to divergent positions between the parties of a tax treaty. In this regard, the updated guidance reiterates that the guidance cannot be relied on to create instances of double non-taxation.

- ▶ **Guidance issued by jurisdictions:** The updated guidance includes examples of guidance on creation of a PE that has been issued by Australia,² Austria,³ Canada,⁴ Germany,⁵ Greece,⁶ Ireland,⁷ New Zealand,⁸ United Kingdom,⁹ and United States.¹⁰

It is important to note that neither the April 2020 guidance nor the updated guidance specifically addresses the issue of a service PE.

Concerns related to change of residence (place of effective management)

This section of the updated guidance is largely consistent with the April 2020 guidance that it is unlikely that the COVID-19 situation will affect the treaty residency of entities. In addition, like the April 2020 guidance, the updated guidance addresses dual residence issues. The updated guidance also includes a new section providing examples of guidance on change of corporate residence that has been issued by Australia, Canada, Greece, Ireland, New Zealand, United Kingdom, and United States.

Concerns related to change of residence (individuals)

This section of the updated guidance is largely aligned with the April 2020 guidance that it is unlikely that the COVID-19 restrictions on travel will affect the treaty residence position for individuals. The updated guidance includes examples of guidance issued by Australia, Canada, Finland, France, Greece, India, Ireland, New Zealand, United Kingdom, and United States, on the topic. To determine the residency of an individual, the starting point is domestic law. If the person is resident in only one jurisdiction, that is the end of the matter but if the person is dual resident, then the tie-breaker rules included in Article 4 of the OECD Model apply. There is a hierarchy of tests, starting with in which jurisdiction does the person have a permanent home available to them.

Moreover, the updated guidance provides further explanation with respect to the two cases described in the April 2020 guidance. As regards the first case, concerning a person temporarily away from his or her home (perhaps on holiday,

perhaps to work for a few weeks) who gets stranded in the host jurisdiction by reason of the COVID-19 pandemic and attains domestic law residence there, it seems likely that the tie-breaker test would mostly award treaty residence to the home jurisdiction. This is because it is probably unlikely that the person would have a “permanent home” available in the host jurisdiction. If the person had a “permanent home” in both jurisdictions, other tie-breaker rules would be applicable (center of vital interests, place of habitual abode, and nationality) and would award residence to the home jurisdiction.

In relation to the second case, concerning a person working in a jurisdiction where he or she is a tax resident who temporarily returns to his or her “previous home jurisdiction” because of the COVID-19 situation, the analysis and conclusions are more uncertain because the person’s attachment to the previous home jurisdiction is stronger. This situation may arise either because the person never lost his or her status as resident of his or her previous home jurisdiction under its domestic legislation, or he or she may regain residence status on his or her return. However, the guidance provides that in cases where the personal and economic relations in the two jurisdictions are close but the tie-breaker rule was in favor of the current home jurisdiction, the fact that the person moved to the previous home jurisdiction during the COVID-19 pandemic may tip the balance towards the previous home jurisdiction. This would usually be decided using the test of “habitual abode,” which refers to the frequency, duration and regularity of stays. The determination of habitual abode must cover a sufficient length of time for it to be possible to ascertain the frequency, duration and regularity of stays that are part of the settled routine of the individual’s life.

This section of the updated guidance also notes that a different approach may be required if the change in circumstances continues even after the COVID-19 restrictions are lifted.

Concerns related to income from employment

The updated guidance includes more elaboration on the income from employment issue than did the April 2020 guidance. The updated guidance first notes that Article 15 of the OECD Model governs the taxation of income from employment by allocating primary taxing rights to the jurisdiction where the employee physically exercises his or her employment. The application of Article 15 to the following fact patterns is considered in the updated guidance:

- 1) Wage subsidy and similar income received by cross-border workers that cannot perform their work due to restrictions
- 2) A worker who is stranded in a jurisdiction where he or she is not resident but previously exercised an employment
- 3) A worker who works remotely from a jurisdiction for an employer who is resident in another jurisdiction

Fact pattern 1

In those cases where the government has subsidized keeping an employee on a company’s payroll despite being unable to work, such income should be attributable to the jurisdiction where the employee used to exercise his employment. These kinds of payments can resemble termination payments, which are discussed in the OECD Model, with primary taxing rights given to the jurisdiction where the employee would otherwise have worked.

Where the source jurisdiction has taxing rights, the residence jurisdiction must provide relief for double taxation under Article 23 of the OECD Model, either by exempting the income or by taxing it and giving a credit for the tax paid in the source jurisdiction.

Fact pattern 2

Due to travel restrictions, some employees have been stranded in jurisdictions other than the jurisdictions in which they usually reside. This situation prevents an employee from leaving that other jurisdiction due to travel limitations where he or she would otherwise have left that jurisdiction and qualified for the exemption on source taxation given in Article 15(2) of the OECD Model.

Given the nature of the public health measures of many governments, it would be reasonable for a jurisdiction to disregard the additional days spent in that jurisdiction under such circumstances for the purposes of the 183-day test in Article 15(2)(a) of the OECD Model. Some jurisdictions may however take a different approach or may have issued specific guidance outlining their approach to such circumstances.¹¹ Taxpayers in this situation are encouraged to contact their local tax authority.

Some jurisdictions have agreed on special treaty provisions with neighboring jurisdictions to which employees frequently commute for work. These provisions allocate the taxing rights in a different way to Article 15 of the OECD Model. Some jurisdictions have agreed to treat the COVID-19 pandemic as force majeure or an exceptional circumstance and,

accordingly, the time spent by the employee teleworking in their home jurisdiction will not be included in the calculation of the maximum work days outside the work jurisdiction limitation for the purposes of the treaty.

Fact pattern 3

A change in the place where the employment is exercised may give rise to a change in the allocation of taxing rights under the tax treaty and also create additional compliance for the employee and employer. The OECD illustrates these situations by providing two examples.

Adjustments in the jurisdiction where an employee exercises their employment can have tax consequences: new taxing rights over the employee's income may arise in other jurisdictions and those new taxing rights may displace existing taxing rights. As payroll taxes are often withheld at source, this results in compliance and administrative costs for the employer and employee. Some jurisdictions have issued guidance and administrative relief to mitigate the additional burden.¹²

Implications

The updated guidance provides a useful analysis of some treaty-related issues that arise because of the prolonged COVID-19 pandemic and is intended to provide more tax certainty to taxpayers. It must be recognized that the guidance is informational only and does not represent the official views of the OECD member countries. It also should be noted that the analysis reflected in the guidance only

covers the OECD Model and only certain PE scenarios (e.g., service PE issues are not specifically addressed). Provisions in bilateral double tax treaties may differ from the OECD Model and such differences would need to be considered in analyzing the result in any particular situation.

It is noteworthy that the language used in the updated guidance is slightly more definite than the April 2020 guidance. For example, the updated guidance provides that an exceptional and temporary change in the location where employees exercise their employment because of the COVID-19 pandemic "should not" create new PEs for the employer, while the April 2020 guidance had indicated that such a situation was "unlikely" to create a PE. Hence, the updated guidance may provide more clarity and certainty.

Nonetheless, the OECD guidance does not address some outstanding questions and in a few cases allows for a flexible approach that may result in jurisdictions taking different positions in the same situation (i.e., it is left up to jurisdictions to include or exclude temporary interruptions when calculating the time threshold).

Taxpayers should closely monitor any guidance from relevant jurisdictions, which may align with the updated guidance from the OECD or which may reflect a different position, in order to assess the potential impact on their operations.

Note that EY maintains a [tracker](#) that provides a snapshot of the tax policy changes in close to 140 jurisdictions around the world in response to the COVID-19 pandemic and that is updated frequently.

Endnotes

1. See EY Global Tax Alert, [OECD Secretariat issues guidance on impact of the COVID-19 crisis on treaty-related issues](#), dated 10 April 2020.
2. See EY Global Tax Alert, [PE Watch: Latest developments and trends, December 2020](#), dated 10 December 2020.
3. See EY Global Tax Alert, [PE Watch: Latest developments and trends, June 2020](#), dated 11 June 2020.
4. See EY Global Tax Alert, [PE Watch: Latest developments and trends, June 2020](#), dated 11 June 2020.
5. See EY Global Tax Alert, [PE Watch: Latest developments and trends, June 2020](#), dated 11 June 2020.
6. See EY Global Tax Alert, [PE Watch: Latest developments and trends, August 2020](#), dated 13 August 2020.
7. <https://www.revenue.ie/en/corporate/communications/covid19/compliance-with-certain-reporting-and-filing-obligations.aspx>.
8. <https://www.ird.govt.nz/covid-19/international/tax-residency>.
9. See EY Global Tax Alert, [PE Watch: Latest developments and trends, May 2020](#), dated 14 May 2020.
10. See EY Global Tax Alert, [PE Watch: Latest developments and trends, May 2020](#), dated 14 May 2020.
11. Sweden takes a different approach and Australia, Austria, Canada, Finland, Germany, Greece, Ireland, New Zealand, United Kingdom, and United States have issued specific guidance on their approach.
12. Australia, Austria, Canada, Finland, Germany, Greece, Ireland, New Zealand, United Kingdom, and United States have issued specific guidance on their approach.

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