

COVID-19: OECD updates its guidance on residence and permanent establishments

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Background

From the beginning of the UK's first lockdown in March of last year we have reported on the impact of the pandemic on individual and corporate tax residence and permanent establishment risk.

In April 2020 the OECD published [guidance](#) on the impact of COVID-19 on double tax treaties (DTTs), including in relation to tax residence, tie breakers and permanent establishments (reported by us in [Tax Talks](#)). When reporting on the previous guidance we noted that further consideration would be needed should the pandemic continue for a significant time. Accordingly, the OECD has recently updated its [guidance](#) to reflect the pandemic's persistence and the risk that some measures taken in response to the pandemic may no longer be described as temporary. Key aspects of the latest guidance as regards residence and permanent establishments are set out below.

Corporate residence

The guidance states that the pandemic is unlikely to change an entity's tax residence under a DTT, reaffirming that a temporary change in location of board members is an extraordinary and temporary situation in response to COVID-19.

In cases of dual residence, the guidance confirms that an entity's place of residence under the tie-breaker DTT provision is unlikely to be affected where individuals are participating in the management and decision-making of an entity and cannot travel because of a COVID-19-related measure imposed (or recommended) by at least one of the relevant jurisdictions.

A particular issue faced by non-UK resident companies because of the travel restrictions was the risk that UK directors of non-UK companies who participate in board meetings and take decisions in the UK could cause those companies to become UK tax resident by virtue of “central management and control” in the UK. HMRC’s guidance in the immediate aftermath of the March 2020 guidance was limited to the short-term and there has been no updated guidance since then. Therefore, businesses should not ignore the potential effect of the long-term of impact of COVID-19 and related travel restrictions on the tax status of their activities outside the UK. For investment managers, a potential medium- to long-term approach may be to consider re-engaging with the UK as a holding company jurisdiction as discussed by us in our [Financier Worldwide](#) article. For further details of HMRC’s approach to company residence in light of COVID-19 see our [Tax Talks](#).

To be a “fixed place” permanent establishment under a DTT, the relevant location must have a certain degree of permanency as well as being at the disposal of an enterprise. Therefore, an employee’s “home office” when working from home will usually not create a permanent establishment where such home working is an extraordinary event in response COVID-19 rather being a requirement of the employer. However, a certain degree of permanence may exist if the individual continues to work from home after the pandemic response measures are lifted. As regards being at the employer’s disposal, the guidance points to the OECD’s Commentary on the issue and distinguishes between circumstances in which it is clear that the employer has required an individual to work from home (for example, by not providing an office for the employee in circumstances where the nature of the employment requires one) and those in which the employee performs most of their work from their home situated in one jurisdiction rather than from the office made available to them in the other jurisdiction. The OECD concludes that the home office in the latter scenario should not be taken to be at the employer’s disposal whereas in the former it could be.

Individual residence

The revised OECD guidance also sets out two situations which might result in an individual’s tax residence changing during the pandemic.

Firstly, an individual may be temporarily away from their home jurisdiction (for example, on holiday or undertaking a temporary work assignment) and become stranded, and tax resident, in the other jurisdiction under its domestic law. The guidance notes that the individual is unlikely to be resident in the other jurisdiction under the tie-breaker provision in the relevant DTT.

The second situation envisaged is where an individual works in a jurisdiction and attains residence there but then temporarily returns to a previous home jurisdiction, meaning that they either lose their residence in their current home jurisdiction or regain their residence in the previous home jurisdiction. The guidance notes that it is unlikely that a person would regain residence status as a result of “being temporarily and exceptionally in the previous home jurisdiction”. Even if residence was regained under that jurisdiction’s domestic law, it is unlikely under a DTT that an individual would be resident because of such temporary dislocation if their connection to the current home jurisdiction was stronger than the connection to the previous home jurisdiction.

HMRC’s guidance on the UK’s statutory residence test (the test that applies to determine whether an individual is resident in the UK or not) states that days spent in the UK due to COVID-19 will be treated as “exceptional” for the purposes of the statutory residence test and under that test 60 days spent in the UK in exceptional circumstances are not counted under the test (reported by us in a previous [Tax Talks](#)).

Conclusion

The guidance reaffirms the OECD’s position of April 2020 and, in our view, should offer some comfort to businesses and individuals concerned about changes in residence and permanent establish risk arising from COVID-19. However, the guidance states that in many circumstances factual determinations by tax administrations will still be required and the guidance does not replace such determinations and, most significantly, each jurisdiction may adopt different interpretations. In particular, in our view, taxpayers should be cautious if setting up non-UK entities or businesses and assuming that they can be managed from the UK during the remainder of the COVID-19-related travel restrictions, since in those cases there will be no track record of overseas management to fall back on.

We will report on any HMRC updates.

Please contact us if you have any queries about how any of the above or how COVID-19 will affect your business.

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