

The tax and social security impact of COVID-19 on cross-border activities

The ongoing COVID-19 pandemic has forced governments to take unprecedented measures such as travel restrictions and the implementation of strict quarantine requirements. As a result of these measures, some cross-border workers cannot physically perform their duties in their country of employment, construction activities are temporarily interrupted and board meetings take place digitally. This situation raises tax and social security issues and may impact the allocation of taxing right between countries. In this updated newsflash, we give you a summary of the possible tax and social security consequences that may apply for certain cross-border activities.

As noted in our prior newsflash, in April 2020 the OECD issued guidance on potential tax issues that arose due to the COVID-19 pandemic. To provide more certainty to taxpayers during this exceptional period, this guidance was updated on 21 January 2021. In this newsflash we will provide more clearance.

It should be noted that the guidance provided represents the OECD's view on the interpretation of the provision of tax treaties. Each jurisdiction may adopt its own guidance to provide tax certainty to tax payers. The Dutch government confirmed though to follow the OECD guidance.

PERMANENT ESTABLISHMENT ISSUES

A permanent establishment ("PE") must have a certain degree of permanency and be at the disposal of an enterprise in order for that place to be considered a fixed place of business through which the business of that enterprise is wholly or partly carried on.

Home office

Due to a travel ban and quarantine situation set by authorities, employees may be forced to work in their home country instead of the country of employment. This raises the question to what extent these activities at home may lead to a PE in the home country of the employee.

In line with its April 2020 guidance, the OECD again confirms that no PE should be in place for individuals who are forced to work from home due to COVID-19. Individuals who work from home are typically doing so as a result of public health measures; it is an extraordinary event and not an enterprise's requirement. Besides, the employer often still provides an office which in the absence of public health measures is available to the relevant employee.

Also, *as further clarification*, the updated OECD guidance now mentions that if individuals continue to work from home after the cessation of the measures imposed or recommended by government, the home office may be considered to have a certain degree of permanence. Yet, that single change will

not necessarily result in the home office giving rise to the presence of a PE, considering that all relevant facts and circumstances should be examined.

Agency PE

The question may also arise whether the activities of an individual temporarily working from home for a non-resident employer give rise to a dependent agent PE. Typically, the activities of a dependent agent will create a PE if the employee habitually concludes contracts on behalf of the enterprise.

Again, *in line with its April 2020 guidance*, the OECD confirms that an employee's or agent's activity in a jurisdiction is unlikely to be regarded as habitual if they are only working at home because of extraordinary circumstances.

However, a different approach may be appropriate if the employee was habitually concluding contracts on behalf of the enterprise in the home country prior to the COVID-19 pandemic, or likewise continues to do so afterwards.

Construction PE

Under the OECD Model Convention, a construction site will normally constitute a PE if it lasts more than a certain period, e.g. 12 months. Due to COVID-19 construction activities could be temporarily interrupted. In line with the prior guidance, it again has been confirmed by the OECD that a construction site PE would not be regarded as ceasing to exist when construction work is *temporarily* interrupted.

Jurisdictions may consider, however, that temporarily work interruptions due to COVID-19 should be excluded from the calculation of time thresholds for construction site PE's.

As mentioned at the beginning of this newsflash, each jurisdiction may adopt its own guidance to provide tax certainty to tax payers.

CHANGE OF RESIDENCE ISSUES

The (updated) OECD guidance also covers the tax implications of a potential change in the *place of effective management* of a company as a result of a relocation, or inability to travel of board members or other senior executives.

It is reconfirmed that it is unlikely that the COVID-19 pandemic will create any changes to an entity's residence status under a tax treaty. Reason for this is that the temporary change in location of board members or other senior executives concerns an extraordinary and temporary situation due to the COVID-19 pandemic.

In case where, despite the OECD guidance, dual residency discussion may arise, reference is made to tie breaker rules of the tax treaty. These rules, most of the time, should ensure that the entity is resident in only one of the jurisdictions.

TAXATION AND SOCIAL SECURITY POSITION OF EMPLOYEES

The updated guidance elaborates more on the income from employment issue than it did in 2020. The guidance notes that some mobile employees are forced to work from home due to a travel ban or quarantine situation as set by authorities and states that this may impact their income tax and social security position. Subsequently, it may lead to reporting obligations for the employer.

In this respect the residence status of the employee under tax treaties may be jeopardized. However, considering the temporary and extraordinary circumstances, the OECD deems it unlikely that the COVID-19 pandemic will affect the residency status of employees. A more regular period of time should be considered in order to determine residence. Nevertheless, working in a different country than the employment country may lead to a change in taxation and social security. Corresponding the April 2020 guidelines, the updated guidance implies that the public health measures should not by itself impact a person's residence status for purposes of the tax

treaty. A different approach may be appropriate if the COVID-19 restrictions are lifted.

Taxation

The main rule under tax treaties is that the employee's salary is taxed in the working country. As a result, employees that normally work in another country than their home country may become subject to taxation in their home country, which could affect their net income. Subsequently, their employer might even have a reporting obligation in that country to set-up a payroll. The latter will depend on domestic tax law of the employee's home country.

In such a situation, it is important to assess the domestic laws applicable and subsequently the tax treaty regarding the allocation of the right to levy taxes on the employee's salary. It may not in all situations be evident what the permanent home of an employee is.

As additional explanation to the earlier guidance, the update holds three possible problematic employment situations:

- » A cross-border worker that cannot perform work due to COVID-19 restrictions. Therefore, the income (and possible subsidies) should be attributable to the place where the employment used to be exercised. Also, as already pointed out under the previous guidance, stimulus packages must be regarded to resemble termination payments and therefore attributable to the place where the employee would otherwise have worked.
- » A stranded worker is prevented from travelling because of COVID-19 public health measures and therefore stays in one jurisdiction. It would be reasonable for a jurisdiction to disregard the additional days spent in that jurisdiction under such circumstances for the purposes of the so-called 183-day test.
- » A worker who works remotely from a jurisdiction for an employer who is resident in another jurisdiction. This may give rise to new taxing rights over the employee's income and can lead to possible compliance costs for employee and employer. Additional coordination is requested in this respect

between jurisdictions to minimize the impact on employees and employers.

Some tax treaties already hold a provision on the situation of cross-border workers, but in the meanwhile the OECD has worked with countries to mitigate unplanned tax implications. Also, as underpinned in the updated guidance, several countries have already taken measures. For example, the Netherlands has agreed with Germany and Belgium on the treatment of home working days.

Social security

Within the EU, the regulations for coordination of social security continue to apply despite the presence of COVID-19. Significantly changed working patterns can lead to a change in social security coverage for frontier employees as well as certain multi-state employees. In general, other types of mobile employees should not be at risk of experiencing changes to their social security coverage as a result of their changed working patterns.

We advise employers to wait for work to be resumed as normal and then assess if there are any changes to the social security that require action, focusing on frontier employees and certain multi-state employees only. The social security regulations provides for solutions to a varied spectrum of working patterns, so employees should be able to maintain their current social security coverage without alteration by applying some of the other provisions in the Regulations.

The Dutch social security authority explicitly indicates that from a Dutch perspective nothing will change even though people are now forced to work in their home country.

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