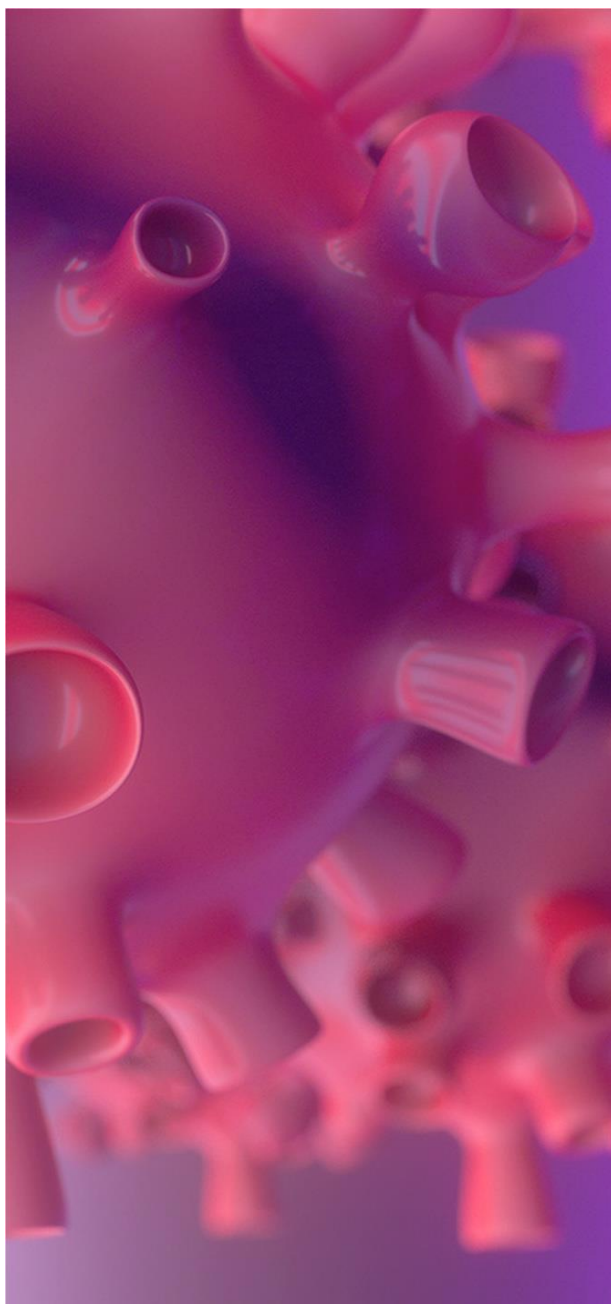

COVID-19 (No. 15): Double tax treaties – analysis by OECD Secretariat

Legal Flash | Portugal

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- **Analysis by OECD Secretariat on the effects of COVID-19 on double tax treaties**



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Current restrictions on the free movement of persons imposed by several countries to tackle the COVID-19 health crisis have temporarily altered how and where employees work.

This unprecedented situation leads to multiple tax issues, namely concerning the existence of permanent establishments, the definition of tax residence for individuals and companies, and the situation of cross-border employees.

On April 3, 2020, the OECD Secretariat published guidelines for the application of double tax treaties during these exceptional times.

In the context of the current COVID-19 pandemic, many States are experiencing a severe health crisis and consequently significant economic problems. Several governments, aiming to support individuals and companies, have adopted unprecedented tax measures that may lead to concerns in the application of double tax treaties.

At the request of many countries, the OECD Secretariat released a document analyzing how COVID-19 affects double tax treaties (*“OECD Secretariat Analysis of Tax Treaties and the Impact of the COVID-19 Crisis”* available [here](#)). This document is part of an extensive series of papers recently published by the OECD, and it has been drafted by the OECD Secretariat itself and not by the organization.

The guidelines included in this document do not differ from the Commentaries on the OECD Model Convention and, in general, embrace the exceptional nature of the situation and recommend solutions aimed at mitigating its impact and promoting interstate cooperation (particularly between the different tax authorities). The document addresses four key aspects:

➤ The concept of permanent establishment (PE)

According to the OECD Secretariat, it seems unlikely that the COVID-19 crisis will have a material impact on determining the existence of PEs throughout the different jurisdictions.

Employees working from home or from other jurisdictions (as dependent agents) do not necessarily lead to the creation of PEs in these jurisdictions, as their homes are not at the corresponding employers' availability. In addition, the place where employees usually perform their functions is more important than the place from where they are currently carrying out their functions due to the current pandemic situation.



Regarding building sites, the interruption of construction works by mandatory lockdown measures does not hinder the creation of a PE, provided the interruption is temporary and justified by an exceptional situation outside the company's control such as the COVID-19 pandemic.

> Tax residence of companies

According to the OECD Secretariat, it is unlikely that this health crisis will affect the tax residence of companies. However, the possibility that double tax residence situations will arise because of the mismatch between companies' statutory seats and the places of effective management cannot be ruled out. In these situations, the conventional tie-break rules should be paramount.

In applying these rules, the Secretariat recommends that (i) if the tie-break rules refer to the Mutual Agreement Procedure, the authorities should consider all the relevant facts and circumstances (including those related to the COVID-19 crisis); however, (ii) if these rules focus on the place of effective company management to determine tax residence, a greater degree of relevance should be attributed to the place from where management is usually conducted, disregarding exceptional circumstances under which such management is carried out from another jurisdiction.

The Secretariat refers to the location of the board of directors as a potential hallmark in determining the place of effective management of the companies.

> Cross-border workers

The State where the work is habitually carried out is entitled to tax salaries paid during this period, even if the worker is physically in a different jurisdiction. The same applies to termination and lay-off payments.

Double tax treaties entered into between border States usually have express provisions regarding cross-border workers, particularly regarding the power to tax their income, as in the double tax treaty entered into between Portugal and Spain. However, as a result of the measures adopted by several States to confine workers to their homes, the State usually competent to tax such income may lose this power. As a result, both employers and employees may be subject to higher tax burdens and additional tax obligations.

In this context, the document calls for flexibility in the application of the special double tax treaty rules for cross-border workers and for additional coordination efforts between the tax authorities of the different States to safeguard against possible tax impacts.



> Tax residence of individuals

Also, as a result of the containment measures, individuals may be stranded in a State other than the State where they are tax residents, which may lead to them acquiring tax resident status in that State, under domestic rules.

However, considering the residence tie-break rules defined in double tax treaties, this crisis is not expected to affect the determination of the tax residence of individuals, namely considering the habitual abode and center of vital interests' criteria. The OECD document also stresses that the tax authorities should consider the exceptional nature of this period.

Therefore, through the legal instruments currently in force, it is possible to minimize the impact that the current restrictions may have on the tax situation of individuals.

Considering the above, it is clear that the OECD Secretariat's position takes shelter in the Commentaries on the OECD Model Convention, given the exceptional and temporary nature of this pandemic, which is beyond the control of taxable persons.

The document also refers to the efforts of many tax authorities (e.g., Australia and the United Kingdom) to clarify the aspects above, particularly concerning permanent establishment and tax residence. These efforts are welcomed and should now be followed with similar initiatives from the Portuguese tax authorities.



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Cuatrecasas has set up a Coronavirus Task Force, a multidisciplinary team that constantly analyses the situation emerging from the COVID-19 pandemic. For additional information, please contact our taskforce by email TFcoronavirusPT@cuatrecasas.com or through your usual contact at Cuatrecasas. You can read our publications or attend our webinars on our [website](#).

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