

COVID-19 and corporate taxable presence

Often a company's tax position will be heavily linked to where it is managed from and where its employees are located. This can drive both the tax residence of the company as well as the question of whether it has a taxable permanent establishment in a second territory. With global travel at a virtual standstill, and typical ways of working massively disrupted, the current environment has the potential to create significant risks in this area.



Corporate tax residence

What's the issue?

Corporate tax residence will often have the place of incorporation as a starting point. However, this will frequently be overridden by rules that can treat a company as resident where either its central strategic management or its effective day-to-day management are located

One of the main risk areas here is that companies which are incorporated outside the UK could become UK resident if a sufficient level of strategic management activity were to take place in the UK. Most obviously this would be in a situation where some or all of the board directors are based in the UK but would normally travel to another territory to hold board meetings. If, due to travel restrictions, directors participate in those board meetings while in the UK, or if strategic decision making starts happening in the UK outside board meetings, then the company could be found to have become UK resident under UK domestic law. It would then be necessary to establish whether there was any overriding double tax treaty to determine the tax residence position or whether the company now had compliance obligations and tax liabilities in the UK as well as potential exit charges from the previous territory of residence.

Conversely, it is also possible that some companies which have historically been UK resident could inadvertently cease being resident in the UK with the potential for this to trigger taxable gains on a deemed disposal of assets. This could happen in situations where management activity that would normally take place in the UK is instead happening in another territory. Given that a number of territories and many double tax treaties look to the day-to-day place of management to determine residence it is important to look beyond just the board meetings of the company.

With both of the issues outlined above it is worth bearing in mind that the current situation may lead to some significant strategic decisions having to be made and that those, when weighed against more routine activity (e.g. approval of accounts) may be more influential in the determination of residence.

How can PwC help?

Up to this point, HMRC have indicated that they would generally see residence as something to be measured over time rather than driven by a specific instance of activity but they have also said that they are bound by the law in this area. More guidance is expected but it is unlikely to offer any general exemption and as such each case will still need to be considered on its facts.

As the impact of COVID-19 looks set to be here for some time it's important to consider ways of ensuring sustainable working practices alongside management of companies' residence positions. PwC can help by:

1. Working with the group to review its corporate structure and governance processes/arrangements to identify potential residence issues.
2. Providing advice about changes that might be made to working practices to help mitigate the risk of unintended residence shifts or other transactions which may reduce the impact of any such shift.
3. Engaging with tax authorities to proactively seek assurance or to defend a company's residence position if challenged, including the gathering of appropriate evidence.



What's the issue?

1. Dependent agent PE

The definition here is not really a time based test but both the historic definition, and the expanded one introduced by the OECD's multilateral instrument, do incorporate the concept of "habitual" actions, whether that be concluding contracts or playing the principal role in a negotiation (and, therefore, if it's entirely new activity in a state it may well not be habitual). As such, it may be that people who are either "stranded" in a territory which is not their normal place of work or that are unable to travel to the place where they would normally conduct contractual activity may increase the risk of a dependent agent PE arising.

2. Fixed place of business PE

This is perhaps the most obvious area of risk although, while various notional "thresholds" are discussed in commentary, it is not generally a strict day count test and really revolves around the more general theme of permanence. Given that there are no fixed thresholds it follows that there is no set policy from HMRC that we might be able to rely on here. That said, it would be necessary for any UK presence to have a sufficient degree of permanence to create a PE and it may be that the temporary nature of Covid-19 arrangements would not meet this criteria although this test should be considered in the round alongside all other group activities in the territory in question. It is worth noting here that in the context of individuals' UK residence (where there are day count tests) there is dispensation for "exceptional circumstances" where individuals have come to the UK and are unable to leave. There is certainly no automatic read-across but it may give some support to any specific requests for a pragmatic approach by HMRC.

(<https://www.gov.uk/hmrc-internal-manuals/residence-domicile-and-remittance-basis/rdrm11005>)

3. Services PE

The UK does not have the concept of a services PE in its domestic law but many UN based treaties will have the concept of services PEs which will generally have a set day count approach (including the Chinese and Indian treaties with the UK). Given the range of territories that are potentially in point it is very hard to generalise but one could imagine that a distinction could be drawn between a service provision which continued over the day count and one where that service provision ceased but individuals remained in-country for longer due to travel restrictions. Again, the key here will be trying to evidence the position as much as possible to give you the best chance of making the argument convincingly.

HMRC has recently indicated in discussions that they may issue further guidance on their thinking on displaced people due to COVID-19 and PE risk, but it is likely that any assessment needs to be facts and circumstances based. If a group's operating model is already potentially risky from a PE perspective then particular care may be needed to monitor the PE position. In addition, it is not clear how overseas tax authorities would assess these exceptional times.

How can PwC help?

PwC can help groups both in terms of managing the risk of creating a PE and also understanding the levels of taxable profit that would be attributable to it. It is important to remember that each case needs to be considered on its own facts but examples of the kind of support that we could provide could include:

1. Working with the group to review its corporate structure and governance processes/arrangements to identify potential residence issues.
2. Providing advice about changes that might be made to working practices to help mitigate the risk of unintended residence shifts or other transactions which may reduce the impact of any such shift.
3. Engaging with tax authorities to proactively seek assurance or to defend a company's residence position if challenged, including the gathering of appropriate evidence.

And finally...

Don't forget that as well as the corporate tax aspects discussed above, the same changes in facts can give rise to indirect tax, personal tax and legal consequences too.